104

THE 1996 BUDGET FOR THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

HEARINGS

BEFORE THE

COMMITTEE ON THE BUDGET
HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

HEARINGS HELD IN WASHINGTON, DC, FEBRUARY 22 AND 23, 1995

Serial No. 104–5

Printed for the use of the Committee on the Budget

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CONTENTS

THE 1996 BUDGET FOR THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

WEDNESDAY, FEBRUARY 22, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
Washington, DC.

The committee met, pursuant to notice, at 9:45 a.m., in room 210, Cannon House Office Building, Hon. John R. Kasich, chairman of the committee, presiding.

Members present: Representatives Kasich, Hobson, Miller, Franks, Nussle, Largent, Myrick, Brownback, Shadegg, and Radanovich.

Chairman KASICH. The committee will come to order.

I understand that Mr. Kemp could not be here this morning. He apparently had a flight that got in in the middle of the night and we will make an effort to reschedule him if it can be worked out. So what we will do is to go to the General Accounting Office, to Mr. Posner and Mr. Wells.

I think it is pretty clear to anybody who has studied the situation at HUD that the government has been able to work itself into an absolutely incredible and untenable position, in terms of being able to manage this whole operation.

I think the testimony of the GAO is important. We are going to have the Secretary tomorrow. I think we are going to have to at some point, I would say to the members of the panel, to Mr. Brownback and Mr. Franks, that we are going to have to look this thing square in the eye and begin to deal with it. It appears to me that no one has been really willing to take these very severe problems on. It is about time we start looking them in the eye and trying to figure out precisely what we are going to do.

The President is speaking to the Democrats and Mr. Sabo suggested we start. So why don't we go ahead. Mr. Posner and Mr. Wells, I cannot tell which one is the chief. The younger one.

Mr. WELLS. For today.

Chairman KASICH. The younger looking one. Anyway, why don't you go ahead and start, Mr. Wells, and we will look forward to your testimony.

STATEMENT OF MR. JAMES E. WELLS, JR., ASSOCIATE DIRECTOR, HOUSING AND COMMUNITY DEVELOPMENT ISSUES, GENERAL ACCOUNTING OFFICE; ACCOMPANIED BY PAUL L. POSNER, DIRECTOR OF BUDGET ISSUES, GENERAL ACCOUNTING OFFICE

Mr. WELLS. Thank you, Mr. Chairman.

Before I start, I did want to introduce Paul Posner, the Director of our budget issues in GAO and I am the Associate Director in GAO's housing and community development issue area, that deals with many of the programs that you are interested in looking at at HUD.

We are pleased to be here today to offer our observations on HUD's fiscal year 1996 budget. Just in the few days since HUD has released its actual numbers, I personally have heard a variety of words to describe the HUD budget request. Some of the words were more on the negative side, like vague, cursory, or inadequate. Or abstract concepts rather than realistic proposals.

At your request, Mr. Chairman, you asked us to take a quick look at those numbers. So just on the surface, when we read the numbers what we see in the HUD budget is $26 billion of budget authority and $26 billion requested in outlays. If you compare this to the fiscal year 1995 levels, this represents approximately a 2-percent increase in budget authority and a 2-percent decrease in outlays, just on the surface.

This morning what I would like to do, if I may, is to focus on two areas. One is the challenges that HUD faces in trying to implement a budget that is based on the reinvention blueprint proposal that they just presented in December; and also, to provide some observations, as you asked us to do, on the budgetary savings that HUD is projecting to achieve over the next 5 years.

But first let me just take a couple of minutes to summarize the major components of HUD's reinvention blueprint. The blueprint itself envisions major changes in the way HUD is organized and the way it delivers its programs, that ultimately is projected to end in three principal results. No. 1, it is attempting to remove public housing authorities from the subsidy programs that have existed and make them compete on the private market. It is also trying to consolidate some 60 major categorical programs into the first year, seven funds next year, and then finally into three flexible performance-based funds in 1998. And thirdly, they are putting together a proposal that would establish an entrepreneurial government-owned FHA.

The bottom line, HUD's reinvention plan will be difficult to implement. It is not going to be easy. Accomplishing that blueprint, on which the 1996 budget is predicated, will require the completion of many significant tasks, an endeavor that will definitely take longer than the 3 years that was originally proposed when they announced their blueprint.

If Congress chooses to support HUD's reinvention strategy, implementing it will require major legislative actions, drastic changes to HUD's regulations, and new ways of allocating funds. It will also place more responsibility on the States and the localities to develop the new plans and ways in which to implement the programs. There will also need to be considerable effort to transform FHA as it is envisioned in the blueprint.

I would just like to highlight just a few examples of some of the difficulties that need to be faced. As we had talked earlier, some of the most radical changes are expected to occur in the planned area of public housing. Under the blueprint, public housing residents will begin to receive portable rental certificates wherever

practical and will permit them to seek better housing elsewhere. With such portability, existing public housing stock, however, will be forced for the first time to compete on the open marketplace. They are currently not competing on the marketplace today.

Major legislative changes are going to be required if that is to be accomplished, such as repealing current requirements that housing agencies must replace housing on a one-for-one basis, anything they demolish or sell must be replaced, and eliminating current preference rules, eligibility rules, as to who is to go in to this type of housing. Also the task of consolidating the many, many individual existing programs that have very clearly defined and spelled out legislative intents.

Also, HUD is going to have to step forth to the batter's box, so to speak, and look at the troubled public housing that exists out there, the public housing authorities, and probably end up in some kind of takeover situation.

Already, HUD finds, as it looks at its plans, that converting all public housing to this type of portable assistance and providing the payments directly to the tenants, within 3 years, is overly optimistic. The latest conversations that we have had with many of the program officials in HUD indicate it may take as much as 8 years to get to a total situation, as they describe in the blueprint plan.

HUD has also proposed a community opportunity fund that will build on the existing community development block grant program that proposes to give States and localities greater flexibility in how they spend the funds. Just today we are releasing a report on the comprehensive community revitalization efforts that exist out there. We visited four communities, we talked to four organizations that have pioneered a lot of new efforts and grassroots efforts at doing a comprehensive assessment of how you do deliver services. They are encouraged and support, on a principle basis, some of the things that they see in the HUD blueprint.

However, HUD's proposals to do all this, again, will take time to implement because while we may have some communities that have a head start, the great majority of these communities will have little experience to draw on. To really make it successful, a lot of comprehensive detailed planning must be done and that is going to require some effort and planning on the localities parts.

Just briefly turning to FHA for a moment, getting to an entrepreneurial government-owned corporation as being envisioned for FHA, if that is what Congress chooses to do, you will need a lot more information to make good valid decisions on whether that is a workable, doable solution.

FHA is currently preparing a business plan and hopes to have a lot of those details which we will be able to look at later this year, I understand in March or April.

While those are just a few of the specific types of problems that HUD faces, and it is certainly not all of the problems that HUD faces, a key challenge facing HUD today is going to be their ability to correct these longstanding fundamental problems of weak internal controls, ineffective organizational structure, and an insufficient mix of staff and people with the proper skills to deliver the kinds of programs that they are talking about, and historically GAO and many of the auditors and private auditors at Price

Waterhouse and others, that have looked at HUD, have seen major weaknesses in their information and financial management systems.

All of you are probably aware history has not been kind to HUD, and they have many difficulties in terms of management areas. That is one of the reasons that we, in GAO, designated HUD as one of our high-risk areas that GAO has been involved in throughout the government.

But my point for this particular assessment of their budget is that, at a minimum, as we look at the blueprint that is currently being designed as the major change and the drastic change in which they deliver their services, you are talking about laying this, these massive changes, on top of their ongoing efforts at trying to get their house in order, in terms of how they deliver to other programs.

And that is a daunting challenge that HUD needs to overcome.

As we work with HUD in trying to get a handle on some of their high-risk areas, we would like to commend HUD. The HUD leadership has put a substantial effort in 1994 into making changes in the agency and how it is managed. And we applaud HUD efforts, but we are also, just conveniently, releasing today GAO's high-risk series of reports. This is the first report on HUD's high-risk areas.

While we point out in the report, from a status standpoint, that they have made major strides in terms of improving some of their management weaknesses, that a lot of their ability to accomplish this still lies ahead. So they are not totally out of the woods yet, in terms of not being a high-risk agency.

The last area I would like to, just as you requested us to do, to briefly comment on some of the savings that HUD projected or proposes in their budget over the next 5 years. HUD is announcing savings in $51 billion in budget authority and $13 billion in outlay savings for 1996 through the year 2000. Mr. Chairman, as you know, these savings are based on a comparison with HUD's current services budget, which does not reflect the reinvention proposal but assumes that these savings will be based on a program and an agency with existing laws and regulations and policies that will remain in effect until the year 2000.

From our quick look, few of the identified savings appear to be directly related to the reinvention proposal. Most of the long-term savings appear to be across-the-board cuts with unspecified technical changes. What I mean by that is the technical changes were listed without much explanation as to where they came from in the actual budget document.

A large portion of those savings in budget authority—almost 40 percent—were short-term savings achieved in budget authority by reducing the length of section 8 contracts, an action that basically defers costs out to later years.

As you will see in our full statement, that you have before you, the budget does not provide a lot of detail on the savings and at this moment we are unable to comment on the accuracy of the numbers.

I would like to make a final point that while these savings, if realized, will in fact, curb the growth in HUD's budget over the next 5 years, the size of HUD's budget is, in fact, very substantial.

HUD's 1996 budget proposals project needs of $149 billion in budget authority and outlays of $145 billion from 1996 through the year 2000.

Also, as shown in our full statement, these amounts are, in fact $51 billion less in budget authority and $13 billion less in budget outlays than HUD estimates would have been required based on current budget services baseline.

However, as you asked, Mr. Chairman, we looked at it also from a different perspective. If you look at it from a perspective of looking at the fiscal year 1995 funding level, and if you froze that level at 1995, what would this budget look like? And by doing that, you would see a budget authority that represents about a $21 billion increase in budget authority and an increase of about $11 billion in outlays for the years 1996 through the year 2000.

In summary, Mr. Chairman, as discussed today, in fairness to HUD, its budget tries very hard to address, in a very difficult budget time, HUD's extremely large financial and social responsibilities. While HUD's budget is directly linked to its recently proposed reinvention blueprint, much of the detailed information that is needed to understand the blueprint is still being developed as we speak.

And I might need to add that, throughout my statement, you will see numerous references to where the information was not available in the budget to make an accurate assessment. I also want to portray that, from our sense, in dealing with the people in HUD, it is not because they are not working hard or it is not because they do not want to provide the numbers. This is truly a complex, difficult agency with a lot of missions and a lot of difficult things that need to be looked at. And anytime you start tweaking in one area, all kinds of things happen in other areas.

So it is very difficult to come up with the numbers and my sense is that they are working hard and hope to have these numbers in more detail available later and we look forward to looking at those numbers.

But what is clear, and I guess the point we want to leave, that even with the savings that are being realized and proposed, the size of the HUD's budget will remain substantial, as currently proposed, through the year 2000.

This concludes my summary remarks and we will be glad to respond and answer any questions. Thank you.

[The prepared statement of Mr. Wells follows:]

PREPARED STATEMENT OF JAMES E. WELLS, JR., ASSOCIATE DIRECTOR, HOUSING AND COMMUNITY DEVELOPMENT ISSUES, GENERAL ACCOUNTING OFFICE

Mr. Chairman and members of the committee, we are pleased to be here today to offer our observations on the Department of Housing and Urban Development's (HUD) budget for fiscal year 1996. In its budget proposal, HUD has requested about $26.3 billion in budget authority and plans the same amount in outlays. Compared with fiscal year 1995 levels, this represents about a 2-percent increase in budget authority and a 2-percent decrease in outlays. The budget reflects HUD's proposed first steps in transitioning to the new agency envisioned in its December 1994 reinvention blueprint.

Our testimony will be based on work we have carried out during the past several years on ways to strengthen HUD's programs, as well as our preliminary analysis of information contained in the President's fiscal year 1996 budget request and the Department's fiscal year 1996 budget summary. Although little detail has been provided, we will also address aspects of HUD's reinvention blueprint. Today I will

focus on (1) challenges that HUD faces in implementing a budget based on the reinvention blueprint within the time frames envisioned, (2) the potential impact of long-term management deficiencies on HUD's ability to implement the blueprint, and (3) observations on the budgetary savings that HUD is proposing to achieve over the next 5 years.

In summary:

Implementing the blueprint on which the budget is predicated will be extremely difficult and will take HUD longer than the 3 years originally projected. If the Congress supports HUD's reinvention strategy, implementing it will require major legislative actions and the design of formulas for allocating funds that are now awarded competitively. It will also place more responsibility on the states and localities to develop new plans to implement the programs and to develop performance measures;

Laying the massive changes envisioned under the blueprint on top of the long-standing departmentwide deficiencies that exist at HUD poses daunting challenges for the Department. The Department's weak internal controls, ineffective organizational structure, insufficient mix of staff with the proper skills, and inadequate information and financial management systems led us to designate HUD as a "high-risk area." In a report issued today, along with reports on the other 17 high-risk areas that we have tracked over the past few years, we point out that HUD's Secretary and top management team have given high priority to correcting these deficiencies; [1] and

The long-term savings projected in HUD's fiscal year 1996 budget request result primarily from shortening the length of section 8 contracts and thereby deferring costs to later years, freezing or reducing program spending levels, and making other unspecified and technical changes. Even with these projected savings, the size of HUD's budget will remain substantial.

First, let me summarize the major components of HUD's reinvention blueprint and the plans for implementing it through HUD's fiscal year 1996 budget.

HUD'S REINVENTION BLUEPRINT AND THE FISCAL YEAR 1996 BUDGET

The reinvention blueprint envisions major changes in HUD's programs and organization, ending in three principal results: (1) removing public housing authorities from subsidy programs and making them compete with the private market; (2) consolidating 60 major categorical programs into 3 flexible, performance-based funds; and (3) establishing an entrepreneurial, government-owned Federal Housing Administration (FHA).

To begin transforming public housing, the 1996 budget proposes to consolidate the funding for public housing into two accounts—one for operations and one for capital projects, such as modernizing viable projects, demolishing nonviable projects, and constructing replacement housing where feasible.

As a first step toward consolidating categorical programs, HUD's fiscal year 1996 budget calls for converting many of them into seven funds that will be merged in subsequent years into the three funds envisioned in the blueprint. The seven funds listed in this budget are intended to shift substantial control of resources from HUD to state and local governments. These funds would support a wide range of activities, such as affordable housing and community-based economic development.

To address the third reinvention objective, HUD's budget envisions a 2-year transition to a new FHA corporation beginning in fiscal year 1996. During this period, FHA's existing insurance programs would be consolidated and a process for restructuring the debt on FHA's current portfolio of insured multifamily properties would begin.

IMPLEMENTING HUD'S REINVENTION PLAN WILL BE DIFFICULT

Accomplishing HUD's reinvention blueprint, on which the fiscal year 1996 budget is predicated, will require the completion of many significant tasks—an endeavor that HUD officials believe will take longer than the 3 years originally projected. If the Congress supports HUD's reinvention strategy, implementing it will require major legislative actions, revisions to HUD regulations, and the design of formulas for allocating funds that are now awarded competitively. It will also place more responsibility on the states and localities to develop new plans to implement the programs and to develop performance measures. Considerable effort will also be needed to transform FHA as envisioned in the blueprint.

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[1] Department of Housing and Urban Development (High-Risk Series, GAO/HR-95-11, Feb. 22, 1995).

REINVENTING PUBLIC HOUSING

Some of the most radical changes to existing programs are planned in the area of public housing. Under the blueprint, public housing residents will receive portable rental assistance certificates wherever practicable, permitting them to seek better housing elsewhere. In addition, under the blueprint, states, local jurisdictions, and neighborhoods would be given the flexibility to design public housing programs to meet their needs while at the same time the public housing stock would be forced to compete with other housing stock in the local area. For public housing, major legislative and regulatory changes would include the following:

Repealing the current requirement that housing agencies. Replace on a one-for-one basis any units they demolish or sell;

Eliminating current Federal preference rules for the occupancy of public housing;

Consolidating a variety of public housing capital programs into a single capital grant to housing agencies;

Consolidating funding for anti-crime purposes, coordinating services, and providing operating subsidies for public housing into a single fund; and

Requiring HUD to assume control over troubled public housing authorities.

Already, HUD is finding out that its plans for converting all public housing to assistance provided directly to tenants within 3 years are overly optimistic. Program officials now estimate that the transition will take at least 8 years. As a result, the two funds into which HUD is proposing to consolidate all public housing programs will continue at least through fiscal year 2002. This timing differs from that projected in the fiscal year 1996 budget, which assumes that both of these funds will be terminated at the end of fiscal year 1997 and folded into a fund for tenant-based certificates in fiscal year 1998.

HUD believes the extension from fiscal year 1998 to fiscal year 2002 is necessary to (1) allow public housing authorities to expend the over $9 billion of modernization and other funds already provided by the Congress so that their housing stock can become competitive with the private market's and (2) prevent the loss of valuable housing stock that might take longer than 2 to 3 years to be made marketable but that residents and local governments agree should be preserved. HUD officials recognize that there is still a substantial backlog of modernization needs and that billions of dollars have been invested in much of this stock. If public housing subsidies were converted to tenant-based certificates before the properties became competitive, the properties would lose vital rental income which may prevent them from remaining available as affordable low-income housing.

CONSOLIDATING ADDITIONAL PROGRAMS

HUD may have difficulty implementing its proposals to consolidate several programs because of the time that may be required for HUD to work out program details and for communities to develop the plans and performance measures needed to implement the consolidated programs. HUD has proposed a Community Opportunity Fund that largely builds on the Community Development Block Grant program and an Affordable Housing Fund that consolidates programs for housing production, rehabilitation, and home ownership. HUD proposes that local communities determine how these funds will be spent on the basis of a community-prepared consolidated plan. HUD has also proposed to consolidate the existing McKinney Act programs for assisting the homeless into a single formula-driven grant with similar planning requirements.

The intent of creating each of these funds is (1) to give states and localities greater flexibility in how they spend funds and (2) to achieve accountability for results. Our report on comprehensive community revitalization efforts, which is being released today, indicates that community organizations would favor this type of funding approach.[2] Community development experts advocate a multifaceted, comprehensive approach to address the complex, interrelated problems in distressed urban areas. Flexible funding facilitates this approach. However, HUD's proposals will take time to implement because many communities have relatively little experience with the comprehensive planning envisioned by HUD. In addition, we found through our work that community development researchers have had difficulty in developing performance measures for revitalization efforts because communities' needs differ and some activities may not be quantifiable.

Developing formulas for allocating funds to programs for assisting the homeless may pose additional challenges. As we reported last year, HUD's earlier efforts to combine selected McKinney Act entitlement and demonstration programs were

[2] Community Development: Comprehensive Approaches Address Multiple Needs but Are Challenging to Implement (GAO/RCED/HEHS–95–69, Feb. 8, 1995).

stopped when disagreements arose over how to design an allocation formula that reflected localities' relative need for homeless assistance.[3] Program consolidation legislation proposed by HUD last year called for allocating funding much as it is allocated in the Emergency Shelter Grant and Community Development Block Grant programs.

TRANSFORMING FHA

Considerable effort will also be needed to transform FHA into the entrepreneurial, government-owned corporation envisioned in the blueprint. For example, for single-family housing, the blueprint proposes that FHA will increasingly rely on third-party partners to design products that meet market needs and to ensure that FHA's insurance and credit enhancement are delivered as efficiently and effectively as possible.

Specific information on the markets FHA will serve, the relationship it will establish with partners in the housing market, and the expected mix of products it expects to offer is, however, not available. FHA is currently preparing a business plan to provide information on these subjects, as well as defining the resource requirements necessary to support FHA's new entity. FHA expects that this plan will be completed by April 1995. Accordingly, the budget figures proposed for the FHA insurance funds are preliminary and will need to be revised after the business plan is completed.

LONG-TERM MANAGEMENT DEFICIENCIES WILL ALSO AFFECT HUD'S ABILITY TO IMPLEMENT THE BLUEPRINT

A key challenge facing HUD today is correcting the fundamental deficiencies that led us to designate it as a high-risk area in January 1994. At a minimum, laying the massive changes envisioned in the blueprint on top of the current initiatives to correct significant management deficiencies poses a daunting challenge for the agency. Furthermore, HUD's ability to effectively implement the reinvention blueprint may be seriously impeded by these longstanding, systemic management deficiencies.

Four long-standing departmentwide deficiencies led to our designation of HUD as a high-risk agency. These deficiencies were weak internal controls, an ineffective organizational structure, an insufficient mix of staff with the proper skills, and inadequate information and financial management systems. Internal control weaknesses, such as a lack of necessary data and management processes, were a major factor leading to the incidents of fraud, waste, abuse, and mismanagement that have come to be known as the 1989 HUD scandals. Organizational problems have included overlapping and ill-defined responsibilities and authorities between HUD headquarters and field organizations and a fundamental lack of management accountability and responsibility. Having an insufficient mix of staff with the proper skills has hampered the effective monitoring and oversight of HUD programs and the timely updating of procedures. Poorly integrated, ineffective, and generally unreliable information and financial management systems have failed to meet program managers' needs and have not provided adequate control over housing and community development programs.

In our high-risk series report on HUD, we point out that HUD's Secretary and top management team have given high priority to correcting these deficiencies.[4] They and other HUD managers and staff committed substantial effort during 1994 to formulating and planning significant changes in the way the agency is managed. We recognize HUD's efforts but note in the report that the mammoth task of effectively implementing these plans still lies ahead.

The extent to which reinvention alternatives are implemented at HUD will be decided by the Congress through the legislative and appropriation processes. However, no matter what form HUD finally takes, strong internal controls, an effective organizational structure, a sufficient mix of properly skilled staff, and adequate information and financial management systems will remain key ingredients to the proper management and control of risks.

HUD'S BUDGET SAVINGS PROJECTIONS

I would now like to comment briefly on the savings that HUD projects in the budget over the next 5 years. HUD's fiscal year 1996 budget summary identifies savings of $51 billion in budget authority and $13 billion in outlays for fiscal years 1996 through 2000. These savings are based on a comparison with HUD's current

[3] Homelessness: McKinney Act Programs Provide Assistance but Are Not Designed to Be the Solution (GAO/RCED-94-37, May 31, 1994).
[4] GAO/HR-95-11.

services budget, which does not reflect the reinvention proposal and assumes, instead, that existing laws, regulations, and policies will remain in effect.[5] Few of the identified savings appear to be directly related to the reinvention proposal. The majority of the long-term savings stem from across-the-board cuts and unspecified technical changes. Another large portion of the savings in budget authority—41 percent—represents short-term savings achieved by reducing the length of section 8 contracts—an action that defers costs to later years. However, from another perspective, the budget request represents an increase in budget authority of about $21 billion and an increase in outlays of about $11 billion for the period 1996 through 2000 if funding were frozen at the fiscal year 1995 level and no adjustments were made for inflation.

SAVINGS IN OUTLAYS

Over 80 percent—$10.7 billion—of the projected $13 billion savings in outlays is to come from three areas:

About $3.4 billion is expected to come from policy changes in rental assistance programs. Savings in rental assistance programs can be effected in various ways, including: (1) reducing the number of households assisted; (2) requiring families to pay a larger percentage of their income toward rent; (3) increasing the income levels of households receiving assistance so that their contributions toward rent would increase; and (4) reducing the maximum rent that the government will subsidize. HUD's budget proposal focuses on the latter two options by (1) giving greater preference to families that are either working or are enrolled in job or education programs, (2) reducing the "oversubsidizing" of private landlords by renewing project-based assistance contracts at lower levels that reflect the properties' lower market value and by scaling back automatic rent increases, and (3) reducing tenant-based subsidies by lowering the allowable "fair market rents." While these actions should lead to reductions in outlays in rental assistance, there will also be costs to HUD's mandatory account associated with restructuring debt on insured multifamily properties so that assistance contracts can be scaled back to market rents. HUD's fiscal year 1996 budget includes $643 million in costs related to such restructuring. However, it offsets these and other costs with $1.66 billion in savings resulting from "program reforms." The budget does not explain what reforms will produce these savings;

Another $3.3 billion reduction in outlays is expected to result from the phased-in reductions HUD expects to make in budget authority over the next 5 years. The budget summary does not provide additional detail on these reductions; and

The largest reduction—$4.0 billion—is expected to come from "technical adjustments and other changes." The HUD budget documents provide little additional information on these savings.

SAVINGS IN BUDGET AUTHORITY

Over 95 percent of the $51 billion savings expected in budget authority come from actions to (1) reduce the terms for section 8 housing assistance contracts, (2) freeze or reduce program spending levels, and (3) technical amendments and other unspecified changes.

Changes in the length of the terms of section 8 rental assistance contracts account for 41 percent—$20.7 billion—of the projected budget authority savings. The changes in the terms of the section 8 contracts represent a reduction in the number of years for which budget authority will be requested rather than a reduction in the amount of assistance to be provided to recipients. Until recently, budget authority for section 8 contracts was typically given out on a 5-year basis. The fiscal year 1996 budget estimate proposes that expiring section 8 contracts be renewed and new "incremental" contracts be awarded for shorter terms—for 2-years up until the year 2000 and 1-year thereafter, according to senior HUD officials. HUD's current services budget assumes that contract renewals will be for 3 years and incremental contracts for 5 years. While this plan reduces the amount of budget authority needed for section 8 contracts in the short term, the initial reductions in budget authority will be made up for in later years as the shorter-term contracts roll over.

Another 41 percent of the savings in budget authority is expected to come from freezing all HUD programs at their fiscal year 1996 levels and making additional across-the-board reductions for major programs, by 3, 5, 7, and 9 percent in fiscal years 1997, 1998, 1999, and 2000, respectively. In addition, about 16 percent is to

[5] Current services budgets that reflect the anticipated costs of continuing Federal programs at present levels without policy or legislative changes are developed as part of the annual budget process.

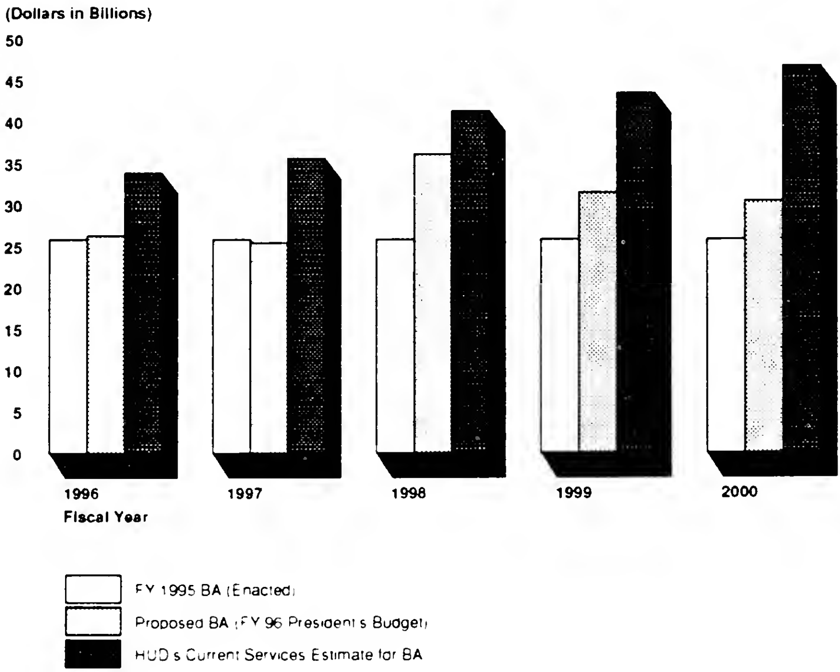
come from technical adjustments and other changes. According to HUD, these reductions are necessary to comply with the discretionary budget caps in law and the extension of these caps through fiscal year 2000 proposed by the administration. HUD's budget summary does not provide additional information on these savings.

While these savings, if realized, will help curb the growth in HUD 's budget over the next 5 years, the size of HUD's budget will remain substantial. HUD's fiscal year 1996 budget proposal projects budget authority of $149.6 billion and outlays of $145.9 billion for fiscal years 1996 through 2000. As shown in appendixes I and II, these amounts are less than HUD estimates would be required if current laws, regulations, and polices were to remain in effect. However, budget authority and outlays for fiscal years 1996 through 2000 are higher than would be needed if funding were frozen at the fiscal year 1995 level and no adjustments were made for inflation. Looked at this way, the budget request represents an increase in budget authority of about $21 billion and an increase in outlays of about $11 billion for the period 1996 through 2000.

In summary, Mr. Chairman, as discussed today, HUD's fiscal year 1996 budget tries to address, in very difficult budget times, HUD's extremely large financial and social responsibilities. While HUD's budget is directly linked to its reinvention blueprint, much of the detailed information needed to fully understand the blueprint is still being developed. Similarly, while HUD's budget projects budget authority and outlay savings over the next 5 years, all of the information needed to assess the accuracy of the savings and to understand their programmatic impact is also not yet available. What is clear is that—even if these savings are realized—the size of HUD's budget will remain substantial.

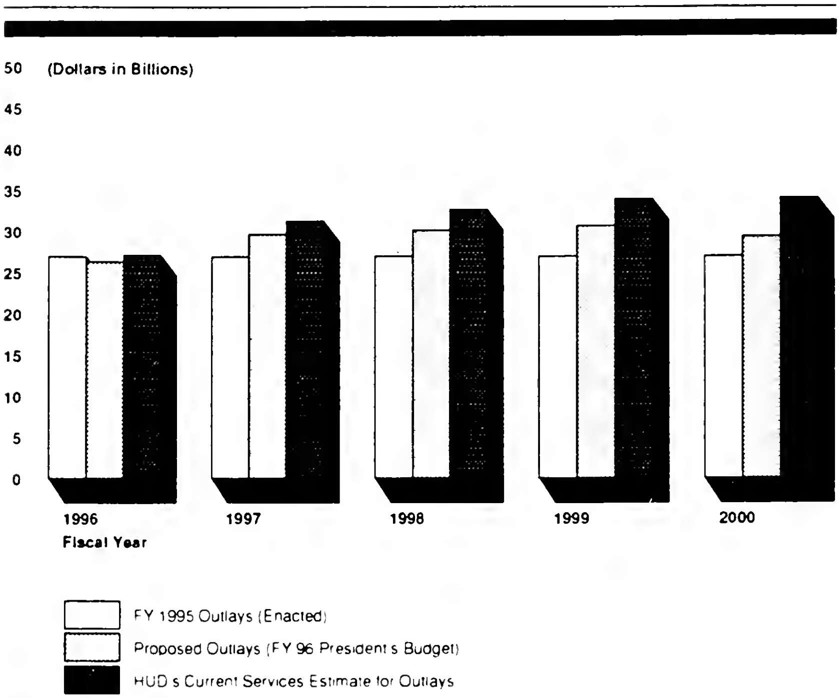
This concludes my prepared remarks. We will be pleased to answer any questions that you and other members of the committee might have. We look forward to working with the committee as you consider issues related to HUD's budget.

APPENDIX I—A COMPARISON OF BUDGET AUTHORITY FOR FISCAL YEAR 1995, PROPOSED FISCAL YEAR 1996, AND CURRENT SERVICES ESTIMATE



Current services budgets that reflect the anticipated costs of continuing federal programs at present levels without policy or legislative changes are developed as part of the annual budget process

Appendix II—A Comparison of Outlays for Fiscal Year 1995, Proposed Fiscal Year 1996, and Current Services Estimate



Current services budgets that reflect the anticipated costs of continuing federal programs at present levels without policy or legislative changes are developed as part of the annual budget process

APPENDIX III—SELECTED GAO PRODUCTS

Department of Housing and Urban Development (High-Risk Series, GAO\HR-95-11, Feb. 22, 1995).

Community Development: Comprehensive Approaches Address Multiple Needs but Are Challenging to Implement (GAO/RCED/HEHS-95-69, Feb. 8, 1995).

Housing and Urban Development: Major Management and Budget Issues (GAO/T-RCED-95-86, Jan. 19, 1995, and GAO/T-RCED-95-89, Jan. 24, 1995).

Federally Assisted Housing: Expanding HUD's Options for Dealing With Physically Distressed Properties (GAO/T-RCED-95-38, Oct. 6, 1994).

Federally Assisted Housing: Condition of Some Properties Receiving Section 8 Project-Based Assistance Is Below Housing Quality Standards (GAO/T-RCED-94-273, July 26, 1994, and Video GAO/RCED-94-01VR).

Public Housing: Information on Backlogged Modernization Funds (GAO/RCED-94-217FS, July 15, 1994).

Homelessness: McKinney Act Programs Provide Assistance but Are Not Designed to Be the Solution (GAO/RCED-94-37, May 31, 1994).

Section 8 Rental Housing: Merging Assistance Programs Has Benefits but Raises Implementation Issues (GAO/RCED-94-85, May 27, 1994).

Lead-Based Paint Poisoning: Children in Section 8 Tenant-Based Housing Are Not Adequately Protected (GAO/RCED-94-137, May 13, 1994).

HUD Information Resources: Strategic Focus and Improved Management Controls Needed (GAO/AIMD-94-34, Apr. 14, 1994).

Multifamily Housing: Status of HUD's Multifamily Loan Portfolios (GAO/RCED-94-173FS, Apr. 12, 1994).

Community Development: Block Grant Economic Development Activities Reflect Local Priorities (GAO/RCED-94-108, Feb. 17, 1994).

Housing Finance: Expanding Capital for Affordable Multifamily Housing (GAO/RCED-94-3, Oct. 27, 1993).

Assisted Housing: Evening Out the Growth of the Section 8 Program's Funding Needs (GAO/RCED-93-54, Aug. 5, 1993).

Government National Mortgage Association: Greater Staffing Flexibility Needed to Improve Management (GAO/RCED-93-100, June 30, 1993).

Multifamily Housing: Impediments to Disposition of Properties Owned By the Department of Housing and Urban Development (GAO/T-RCED-93-37, May 12, 1993).

HUD Reforms: Progress Made Since the HUD Scandals but Much Work Remains (GAO/RCED-92-46, Jan. 31, 1992).

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Chairman KASICH. Thank you, Mr. Wells. Mr. Posner, do you need to make a statement?

Mr. POSNER. No.

Chairman KASICH. Good. Mr. Wells, I am a little confused about the thrust of your testimony. You know, I guess you feel a little torn, like I do, that HUD has tried to make an effort to get somewhere. But from what I understand, the General Accounting Office essentially felt as though there are giant holes in getting—in other words, we know we want to get to the other side of the cliff, and we have this big gorge separating where we want to get to. And we know we want to get over there, but there is no bridge to get there.

So we talk about the fact that we are dreaming about being on the other side, but we do not know how to get there. Does that not essentially sum up GAO's feeling about this budget proposal?

Mr. WELLS. Well, I think in my testimony we were trying to give you a perception that HUD is trying. They have put something on the table and now they are scrambling hard to backfill and look at what the impacts are going to be, but the numbers have not been available to GAO as of this moment, to make an assessment.

Chairman KASICH. You sound like a charitable guy, and I do not really want to work over the administration necessarily on this, because frankly this has been going on for about 30 years, hasn't it? These problems?

Mr. WELLS. Since 1965 in HUD's case.

Chairman KASICH. I am talking about the fact that we take public housing, we own the mortgages on the privately owned, the section 8 housing. In many cases they charge more than what they should charge. Their rates are far above the rates that are charged with other houses in the area. Yet we cannot tell them to reduce their mortgage rates because if they reduce them and they go bankrupt, we hold the mortgages and the mortgages are not worth the value of the property, right?

Mr. WELLS. That is correct.

Chairman KASICH. And in the area of the public housing, I mean we do not know how we are going to get out of that. We have got all this maintenance backlog and we do not have the money to do it, correct?

Mr. WELLS. That is correct.

Chairman KASICH. So here we are holding a bunch of properties that are valued far below the mortgage that we have underwritten on those properties, the people who own these properties are charging more than what the market ought to be permitted to charge. We cannot cut the rates because they say they will go bankrupt. And if they go bankrupt, the worse thing happens, we get the property and it is not worth the value of the mortgage.

Now they say they want to get to vouchers by 1998 but they, of course, do not tell us how they are going to get there; is that correct?

Mr. WELLS. The details are still being worked out, yes, sir.

Chairman KASICH. Wait a minute, the details are still being worked out. That is like saying I am going to fly out this window, I just have not figured out the details yet.

We are saying the details are not there. Is that not kind of like an understatement? I mean, they say they want to have vouchers. How are they going to deal with these privately held mortgages that we hold, or these privately run houses that we hold the mortgage to, how are they going to deal with that? And what should we do about it, Mr. Wells?

Mr. WELLS. Those are excellent points that you have made, and particularly in two areas that I would like to touch on. If I could go a moment——

Chairman KASICH. See, you are being charitable again. Go ahead.

Mr. WELLS. I would like to go back, you are 100 percent right in terms of commenting about the disastrous situation that HUD has gotten itself into. And one of the areas that they are looking at is this mark-to-marketing proposal, to get a handle on the extreme excessive amount of Federal subsidy that is going to landlords because the rents are so much higher than market.

Right up front, I think the people in leadership in HUD recognize that this is an intolerable situation and absolutely something must be done. They put on the table a proposal to go to some kind of mark-to-market proposal. We commend HUD for at least recognizing that something must be done and the existing situation cannot continue.

Believe me, this kind of situation does not exist in private industry because they would not have let this happen. So from a standpoint of we cannot sit by and leave everything in place, you are right because all of the properties would go into default and we would have a massive situation where none of the properties would be available to meet any kind of housing needs.

So I think our bottom line is that we commend HUD for doing what private industry has always done, and that is to reevaluate, ask for legislation, whatever it takes, to get this into a doable situation so we can stop making these excessive subsidy payments to these landlords.

The other comment that you asked, will the voucher system work? Will the certificates be available and will it work? The lack of details that I responded to, Mr. Chairman, relate to the wide variety of public housing, the wide variety and the condition in which so many of these assets out there are in. Some of them are in deplorable, vacant, uninhabitable situations with some very good housing. Some of the difficulties—to really determine whether the vouchers will work or not work—almost requires an individual property-by-property assessment to make the determination as to whether, in the year 1996, 1997, 1998, vouchers will in fact solve the problem.

So that was my comment in terms of the details, that they do not know what condition many of their properties are in or whether they will ever get to market.

Chairman KASICH. So they do not have the inventory of precisely the situation the Federal Government finds itself in.

Mr. WELLS. That is correct. That has been a longstanding problem.

Chairman KASICH. So how can they have a plan in 1998 that does not have the details about how to get us out?

Mr. WELLS. That was identified as a high-risk area and that is what we were looking to HUD to do—to get the information management systems in place, to let them get out and do this.

Chairman KASICH. Did they do that?

Mr. WELLS. They are working on it. It is not in place yet.

Chairman KASICH. Well, like I say, I think anybody that got that job would be in a position—I mean, you have got to be fair about these things. You know what I am concerned about, Mr. Wells, and then we will go to Mr. Franks. Let me ask you this, is there not a point in time when we simply have to stop having good money chase bad? Is there not a time when we have to do, as they say, cut your losses and make some definitive policy moves to try to get out of this mess?

Mr. WELLS. Yes, sir. Major changes and reforms are needed the way HUD currently operates. HUD has put a proposal on the table, and I assume there is room for many more proposals.

Chairman KASICH. I do not mean reforms. I mean a shock, in terms of this is what we are going to do. Instead of kind of dancing around the problem. Are we not still dancing around the problem, because we do not have the details of how we are going to get out of this fix? Is it not time to just lay it out there?

Mr. WELLS. I think that is an appropriate start, yes, sir.

Chairman KASICH. Mr. Franks.

Mr. FRANKS. Thank you, Mr. Chairman.

Mr. Wells, I recognize that you do not manage this agency.

Mr. WELLS. Thank you.

Mr. FRANKS. You merely try to monitor its activities. But if anybody was watching, if this would have been televised on C–SPAN, I think all of us recognize that the American people are essentially compassionate and they want progress made to improve the quality of life for the tenants in public housing, and they want certainly to achieve the goal of home ownership outside of government-sponsored programs as quickly as possible.

But if people were to have listened to your colloquy with the chairman, I suspect that they would conclude that perhaps taxpayers are not getting their money's worth from the moneys being invested in the Department and the programs managed by the Department. You have cited a whole host of problems in your testimony. On pages 5 and 6 you talk about the long-term management deficiencies that were cited in previous reviews.

Following up on the chairman's line of thought, as this new reinvention blueprint has now been overlaid on top of what you and your agency have identified as a series of long-term systemic management problems, is this not perhaps a very appropriate time to scrap the agency as we have known it to date and build a new agency with a newly modernized, reconfigured mission?

Mr. WELLS. Fortunately for me, as an auditor and an investigator, I do not have to make the policy calls about whether that is the appropriate decision. But we are certainly in a position to give you the benefit of the facts, figures, and numbers that we found in terms of what is working well and what is not working well. Ultimately what reform or what program exists, whether it be HUD or someone else, or some other Federal agency, or whether it be the

State and local communities, what form that takes is appropriate to be discussed in these types of hearings.

The difficulty and what also needs to be remembered is the serious implications that whatever changes we make, whatever changes the Congress chooses to make in delivering these types of services, there are—as you mentioned earlier—that population that has needs that need to be met in some kind of housing assistance. And history has shown that the existing programs that we have in place in HUD have not worked that well, nor have they been very cost effective.

Mr. FRANKS. Mr. Wells, let me come at this from a different perspective. As an auditor, does the current configuration and management practices at HUD impede its ability to adapt to a new mission statement?

Mr. WELLS. Yes, sir, they do.

Mr. FRANKS. Thank you, Mr. Chairman.

Chairman KASICH. Thank you, Mr. Franks. Mr. Brownback.

Mr. BROWNBACK. Thank you, Mr. Chairman, I appreciate that. And thank you very much for being here, Mr. Wells. I have a couple of questions.

You had stated at one point, I think in answer to a question, that the private sector would not have let this situation get this way. What would have happened in the private sector with the housing that the Federal Government has or supports at HUD, or through HUD?

Mr. WELLS. Let me just give you the initial scenario as to how HUD got itself in the situation. A decision was made that they would go into a severely depressed, needy community in a downtown urban center, for instance, and put up a $1-million building to meet a housing tenant need. That $1 million building incurred a debt service load. We provided the mortgage, we insured the mortgage for it. It is a building that is costly to operate.

You combine the debt service, the operating cost to run the building, and you put a landlord in there and agree to insure his loan for 40 years. And then in turn, for him to make that property pay, he has to charge $800 rent. But yet surrounding him, market rents in that particular neighborhood might be $400 a month. As you well know, the situation the Government gets into is that the tenant is paying 30 percent of his income. Let us say he is paying $200 of that for rent. The difference between the $200 and the $800, the rent that the landlord needs to make the property work, is the subsidy that the Government has got itself into paying.

Private industry would not have made those decisions in the first place.

Mr. BROWNBACK. So we gave them the money, the insurance, the tenants, and we subsidize the tenants and we told him you make this work now.

Mr. WELLS. And we told him what kind of tenants to put in there.

Mr. BROWNBACK. And it has not worked?

Mr. WELLS. It has not worked.

Mr. BROWNBACK. How would you get out of that, then?

Mr. WELLS. That gets to the heart of the recognition that this cannot continue to go on because of the budget and the outlay im-

plications this has in future years. Can we continue to have that kind of money paid indefinitely into the future? And the answer is "no."

So that gets to the heart of going in and making a realistic assessment of what the property is worth, what it commands in the fair market, and writing down that landlord's debt, taking a hit.

Mr. BROWNBACK. And just selling it?

Mr. WELLS. Not selling it, keeping the property but writing it off to the insurance fund, in the mandatory account.

Mr. BROWNBACK. But basically you are saying cut your losses the way a private company would cut their losses on a bad deal?

Mr. WELLS. That is correct. That would be one alternative.

Mr. POSNER. If I could just add, one of the ironies that we face at the Federal level is in order to reduce spending sometimes you have to increase spending elsewhere, which is what the tie-in with the FHA fund is. I think what the strategy and the budget is, essentially rather than letting those additional costs go unfunded, which was apparently an initial proposal, they have decided to seek a pay-go offset for those additional costs which will prevent the deficit from going up as a result.

So in other words, you are going to take a savings by reducing the section 8 housing payment, and you are going to offset the increases to the fund on the pay-go side, although the offsets have not been specified yet.

Mr. BROWNBACK. As an auditor though, you think it is time to cut our losses on many of these and let us move on down the road?

Mr. WELLS. Yes, sir, whether it is that option or some other options to get at getting it down.

Mr. BROWNBACK. Director of the OMB Rivlin has suggested, prior to being the Director of the OMB, that we should not even be in the housing business at the Federal level. Has GAO looked at that concept, relative to the percentage of housing provided to the less fortunate by State, local, private groups versus the Federal Government and then come up with any sort of recommendation or conclusion in that same area?

Mr. WELLS. The short answer is "no," sir, we do not have a report that spells that out. I mean, I can give you some general statistics about what outside interests have documented, that there is an eligible, needy population out there in the neighborhood of 35 million families and individuals who are in some kind of a rental situation. Of those, about 14 million represent the need that is out there for some type of assistance in terms of getting decent, affordable housing.

HUD, right now, through all of its programs since 1965, is serving approximately 4.2 million of that 14 million that is in need. The 4.2 million has been determined based on the amount of money that is available for HUD to provide housing assistance.

Mr. BROWNBACK. Would it be possible for us to simply voucher that 4.2 million from the Federal level and be rid of a lot of the other whistles and bells that have grown up around this?

Mr. WELLS. I think, on a very high scale, that is the principle that is being proposed to the HUD reinvention blueprint, the strategy and direction is to get there.

Mr. BROWNBACK. Thank you, Mr. Chairman.

Chairman KASICH. The gentleman has exhausted his 10 minutes. The gentleman from California, the little old winemaker, Mr. Radanovich.

Mr. RADANOVICH. Thank you, Mr. Chairman.

I just want to get your comments. It seems that the whole idea behind HUD and providing housing for those that do not have it is kind of like a stopgap measure. Is there any idea out there to eliminate the need, to where you get people to the point where they can get their own housing, rather than dealing with the symptoms? Have you ever thought of getting to the cause? What is causing this and how might you be able to get out of this business and get it into the private sector, so that we do not have to deal with it anymore?

Mr. WELLS. Mr. Chairman, some of the information that you are asking is the kinds of things that are being addressed at the grassroots level with the comprehensive approaches to dealing with not only the housing assistance problems, but other problems of the individual families, whether it be jobs, whether it be health care.

There are pilots out there that have been very successful, that the private sector has picked up and worked. But across the board, we at GAO have not done a major assessment of that.

Mr. RADANOVICH. I guess in my opinion, I think you would have more success teaching a cow to fly than you would having government in solving this problem and getting rid of it. That is why I just want to state for the record that I am absolutely for privatizing this whole function. Thank you.

Chairman KASICH. Mr. Shadegg.

Mr. SHADEGG. Thank you, Mr. Chairman.

You indicated that your task is to look at what is working well and what is not working well. I have heard a lot about what is not working well. I understand that notwithstanding the fact that we have spent billions of dollars, we have got—as I understand your testimony—a population that we are serving of 4.2 million and a population of 14 million that is documented in need?

Mr. WELLS. Meets eligibility requirements for many of the programs, that is correct.

Mr. RADANOVICH. And in response to Mr. Brownback's question, he said could we simply not address this by vouchering and you said well, that is kind of——

Mr. WELLS. The 4.2 million serviced?

Mr. RADANOVICH. Right. Could we not address that problem by vouchering, and I think his term was get rid of some of the bells and whistles, by which I took it to mean a lot of the administrative costs that we are currently losing?

Mr. WELLS. Vouchering has proven to work successfully in individual cases. In other cases, it has not worked well. I think this is still a question that cannot be fully answered. Can needs be met totally? I am not sure they can because there are handicapped individuals, there are elderly individuals that may not be as mobile and just giving them a voucher and saying go find something may not be the best solution or a workable solution. So there are a lot of questions that still have not been answered, but that is the goal.

Mr. SHADEGG. From your earlier testimony, and I thought you walked through it fairly clearly, you pointed out how government

came up with this idea that needed to provide housing. It decided to subsidize a huge expensive building in a low-income area. They went in, private investors built the building; we subsidized it, and we underwrote it all. And now we are facing huge losses. I do not know that I have heard the dollar value of those losses.

But it seems to me you pretty clearly stated that what we are doing is not working well and it is not very efficient, it is not very effective. That is, we are wasting millions of dollars and we are not serving the need.

So it seems to me, to follow up on the chairman's original point, that we need rather radical solutions rather than going with some tinkering here to tweak what we have already done. I, quite frankly, think your testimony about the way government went at this at the beginning illustrates the point that government does not do this well when it tries to plan it out, particularly in housing markets, where it competes with the private sector; is that not correct?

Mr. WELLS. That is correct. I do not disagree. Major changes are needed. I agree tinkering is not going to get us that far.

Mr. SHADEGG. Thank you.

Chairman KASICH. Ms. Myrick.

Ms. MYRICK. This is partly hypothetical, I guess in one sense, but we talk about using a voucher system in the future, as part of this reinvention, and where we are going to be going with HUD. And as a former mayor of a city who dealt with a lot of this on a regular basis, and we have a pretty good housing authority in our city compared to most of them, my concern is that if we do—I noticed throughout the information, we are talking about modernizing existing public housing so they can compete with the private sector and we do not get stuck with all this stock, et cetera, et cetera. And everybody's main concern, of course is providing housing. That is understood. Nobody is going to throw people out in the streets.

But my concern is very simply that it has been my experience in the past that if a person has a choice, through a voucher, or just a choice in general, of whether they live in a public housing project—or community, as we called them—or they can go into the private market someplace and live, they are going to go into the private market and live.

And so we go through this process of modernizing these multifamily units so they can compete and people will not live there anyway. This is just perception partly, but it is true, that they will not do that.

So again, I come back to the same thing. Why are we even going through the process? I mean, I know we are going to get stuck with a lot of property, but we are going to get stuck with it anyway. So should we keep on continuing to pour this money down the rathole?

I really have a lot of trouble with that because it just seems like we are continuing to do the same thing we have done for years, to no avail, and should we not just hang it up?

Mr. WELLS. I agree with you 100 percent that that is a question that the Congress needs to ask of HUD, to ensure that they make the kinds of decisions that you are talking about, the kinds of decisions that says the existing piece of property stock is not worth modernization, will never compete with the private sector, and should be terminated at this point, without modernization.

Ms. MYRICK. The problem with asking it of HUD, generally, when you are talking about an agency that you are talking about putting out of business, they really do not want to make those choices to put themselves out of a job. So how do you get around it, other than us dictating it, right?

Mr. WELLS. It is a circle, yes, ma'am. Somebody must make those decisions.

Ms. MYRICK. Thank you.

Mr. HOBSON [presiding]. Representative Largent.

Mr. LARGENT. A couple of questions, just for my information. Explain what mark-to-market is?

Mr. WELLS. Mark-to-market is basically determining what the existing current market value is of that particular piece of property. Forget how much is remaining on the mortgage, forget how much it costs to build, what is it worth today if you had to sell it? If you have a $1-million building but it is only worth $400,000 or $500,000, you mark-to-market, you basically change the amount of mortgage that that landlord has to pay and recalculate it based on half a million instead of $1 million. That is what mark-to-market basically is.

Mr. LARGENT. Also, in the testimony that I have before me, it says HUD is finding out that its plans for converting all public housing to assistance provided directly to tenants within 3 years are overly optimistic. And it goes on to say that program officials now estimate that the transition would take at least 8 years. Why is that?

Mr. WELLS. A number of reasons, but getting at—there is approximately $10 billion worth of modernization funds that have already been approved, appropriated and sitting, that need to be expended on some of these poorly maintained, ill-repaired property, to basically allow them the time to put the money into the buildings to get the building up to standard. To make sure they all have doors and the faucets are not leaking, so that they are attractive enough so that when we basically cut this landlord loose to compete in the marketplace, his properties are attractive enough that someone would be willing to pay the rent to live in them. And that they cannot accomplish in 3 years.

That is the biggest problem, giving them more time to compete, to get them into a position where they can compete.

Mr. LARGENT. In this move, this transition to go from subsidizing the developer or the landowner to moving to a voucher, why can't we just move to—I am sorry Jack Kemp was not here today, but he talks about moving to ownership, allowing the tenants to actually become owners of the property themselves, and the sort of moral transformation that takes place in one's life. Why can't we be talking about moving in that direction?

Mr. WELLS. I agree, I wish Mr. Kemp were here today, because that really is his field and something that he is very much interested in, and personally committed to make happen. There are any number of HUD programs that have been piloted and tested and, as I understand it, and I am no expert in the particular area, but it really comes down fundamentally to the people that we are dealing with have annual incomes of between $6,000 and $8,000.

It is the difficulty of getting the amount of money that is needed to get into a kind of a home ownership situation is just extremely, extremely difficult.

Mr. LARGENT. Are you familiar with the Habitat for Humanity that is a private sector organization that is providing for low income——

Mr. WELLS. Yes, sir, I am aware of what its mission is and what it is attempting to do on somewhat of a small scale, or a large scale, depending on how you look at it.

Mr. LARGENT. Is it possible to move HUD in that direction? I mean, away from the Federal controls and more into the private market, localized, community-based programs?

Mr. WELLS. My sense is that HUD has gotten the message, that the way in which they tried to deliver housing assistance over the years has not worked, has not been very successful. I think what I see, that they want to consolidate, and they want to go to more of a block grant, and they want to push the delivery system down to State and local and nonprofits is the right way to go. And I think they have seen the light.

Mr. LARGENT. I would just conclude by saying I appreciate both of you coming here today and I appreciate the information that you have given to us because what I hear you saying today is you are not trying to defend a program that clearly has failed and that has to be addressed.

I am also disappointed. I think the people that are present here today will be the party that will be castigated for lack of compassion as we move to make the reforms that are necessary within HUD, but we are the ones here at the hearing.

Thank you.

Mr. HOBSON. The gentleman from Florida, Mr. Miller.

Mr. MILLER. No questions.

Mr. HOBSON. The gentleman from Iowa.

Mr. NUSSLE. No questions, Mr. Chairman.

Mr. HOBSON. I was not here for much of your testimony, but I used to work in the area as a mortgage banker many years ago. I can remember back when this agency was a contributor rather than a negative or a cash cow. I guess I would say, what happened? Do you remember reading about those days? You are too young.

Mr. WELLS. I would like to say that I still see HUD as a contributor, even though it has its problems and it has its programs that have not been 100 percent successful. I mean, just take FHA, which you are probably well aware. There is almost $400 billion worth of insurance out there. HUD has done a remarkable job of making home ownership affordable for a lot of people that would not have houses if they were not there.

Mr. HOBSON. What went wrong?

Mr. WELLS. What went wrong is they are not saying that to continue doing what they are doing, it is going to cost $150 billion for the next 5 years in this country. It is going to be awfully difficult to continue that kind of expenditure level if we are not achieving the same kind of results that you would expect from that kind of expenditure. That is what happened.

The delivery systems have not been all that cost effective and there ought to be an opportunity to relook and rethink, in terms of how we deliver HUD housing assistance services.

Mr. HOBSON. And redesign that?

Mr. WELLS. And redesign them.

Mr. HOBSON. Who should do that? I guess my problem is if this outfit has not been able to do it, should we find a new ability to—I am not sure the Congress is very good at this, either. Who do we get to design us a model that will have expectations of one, solving some of the social needs that we want to solve with these programs and make them work; but two, achieve the kind of goals that we want as far as being effective? Where would you turn to do that?

Mr. WELLS. I do not have the answer to who, but I agree 100 percent that those are the questions that need to be asked. And I think the starting point for fixing HUD is for a sitdown session that says what truly is the Federal Government's role in housing? Where do we start? And what should be the mission?

Right now, I think HUD is a collection of programs that have just gone off in all kinds of directions, and they are following the legislative direction that they have been given over the years, and that has become unworkable, unaffordable, and it is not doing the service to the primary people that we want to assist. So it is time to rethink the Federal Government's role in housing.

And once you decide that, then I think you can start to answer the question who should do it? Maybe it should not be done at HUD. Maybe it should be done elsewhere. But until you know what the mission is, then you can go out and achieve it and decide who should do it.

Mr. HOBSON. I am hoping that somebody listening or talking can come up with some ways to do this. We have certainly, in my opinion, not had a lot of consistency. We have had a lot of experimentation and, as we say in the State legislature, a lot of seeds planted that grow into trees—scrub trees in a lot of places and not trees of lasting value.

It seems to me that one of the things that we ought to do is take your advice, but I am not quite sure how we do that in this environment that we have. We tend to be crisis managers a lot of times, rather than long-term, thoughtful planners and managers of our programs. Then we get these different things that have been added over the years and, to me, have just killed this agency, which I think could do a lot of good.

I want to turn this back to the chairman, if I can get him back here in a minute, and let him wrap it up. I thank you for coming. The chairman will now resume the Chair.

Chairman KASICH [presiding]. Thank you.

Mr. Wells, we are going to have to use your expertise and also Mr. Posner's on this, because we intend to, we hope to kind of take this thing on at some point. I know that Mr. Lazio is involved, and there is just a lot of thought.

But I think at the end of the day, and we do not want to keep this thing drifting, we really have to try to pin some things down. So we are going to really need your folks help and expertise in this whole thing.

Mr. WELLS. We will be glad to help.

Chairman KASICH. Thank you all very much. The hearing will be adjourned.

[Whereupon, at 10:35 a.m., the committee was adjourned.]

THE 1996 BUDGET FOR THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

THURSDAY, FEBRUARY 23, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
Washington, DC.

The committee met, pursuant to notice, at 10:20 a.m., in room 210, Cannon House Office Building, Hon. John R. Kasich, chairman of the committee, presiding.

Members present: Representatives Kasich, Shays, Herger, Bunning, Allard, Miller, Lazio, Franks, Nick Smith, Inglis, Hoke, Molinari, Nussle, Largent, Myrick, Brownback, Bass, Sabo, Coyne, Costello, Johnston, Orton, Pomeroy, Olver, and Rivers.

Chairman KASICH. I think we can go ahead and get started.

I don't know what order you want to go in. John Weicher from the Hudson Institute has spent a lifetime studying this operation and he has a lot of very good insights.

Ron Utt from the Heritage Foundation has been involved in innovative changes in the way in which we ought to do public policy forever. He has a Ph.D. in economics from Indiana University, so he is, of course, in mourning, Mr. Bunning, with what is going on in the Big Ten this year, but he is also a very bright man.

Mr. Weicher has a Ph.D. from the University of Chicago. He has been on the faculty of Ohio State, and that is probably why I like him so much.

Whoever wants to go first, fire away.

STATEMENT OF DR. JOHN C. WEICHER, SENIOR FELLOW, THE HUDSON INSTITUTE

Mr. WEICHER. I guess we will go in reverse alphabetical order, Mr. Chairman.

Thank you very much for inviting me to testify before you today. I am especially glad to be here because this year offers an historic opportunity in housing as well as other areas of public policy and your deliberations on the 1996 HUD budget, I hope, will be an important milestone on the path to a fundamental restructuring of HUD's activities.

I should begin by saying that I am not here to speak for the Hudson Institute, which is a nonprofit policy research organization, or for anyone else except myself on the basis of my own knowledge and experience at HUD. I have served at HUD in three different administrations over the last 20 years, most recently as Assistant Secretary for Policy Development and Research under Secretary Kemp and President Bush from 1989 to 1993.

I am an economist. I not only have my Ph.D. from Chicago, but I have to tell you, I have my B.A. from the University of Michigan. I have devoted my career to the study of housing and urban problems, and I did, indeed, teach for 10 years at Ohio State before coming to Washington. The University of Chicago dropped out of the Big Ten in 1946, so we don't pay a lot of attention to what happens there.

I am going to discuss the HUD budget in the context of the administration's Reinvention Blueprint for HUD, which was released last December. The blueprint advocates some policies which were developed in the Reagan and Bush administrations, and, for that matter, in the Nixon and Ford administrations. I think Congress can do better, still. The blueprint contains some bad ideas, too, but it certainly changes the political landscape.

Unfortunately, the changes in the blueprint don't make much of an appearance in the budget. That is because they are to be phased in gradually. The initial stages of the blueprint just fold a number of existing programs into block grants without any reduction in funds or any change in policy, and that is about all you see in this budget. The real changes are scheduled to occur in 3 years, during the next administration and during the next Congress.

As I was reading the budget, I was reminded of a prayer of St. Augustine's in the confessions. "Lord, give me chastity and continence, but not just now." Reform me, but don't reform me for 3 years, please.

I think you can enact more significant changes in the budget and in housing policy now. You don't have to wait 3 years. The budget has $26.3 billion in both BA and outlays. I think you can save over $2 billion in BA and, at the same time, you can help HUD to run its basic programs more effectively.

I will start with the most dramatic and most positive proposal in the blueprint, which is to convert public housing and other project-based assistance to housing vouchers or certificates. The money that now goes for public housing operating subsidies and modernization would go, instead, to tenants in the form of a voucher. They could choose whether to stay in public housing or move to private housing.

The blueprint would force PHA's to compete for tenants. They would no longer have a captive tenant body. It would subject them to the discipline of the housing market. It would also let low-income families make their own decisions on where they want to live. The same policy would apply to privately owned projects as their current contracts with HUD expire, and all future incremental assistance would take the form of vouchers.

This proposal makes sense in budget terms and in policy terms. Housing vouchers and certificates work for all kinds of families in all kinds of markets. Over 1.1 million families now receive them. Over half of those families are either African American or Hispanic. On a scale of 1 to 10, two-thirds rate their housing at 8 or better.

Also, project-based assistance can be turned into vouchers at no additional cost and, I think, at some savings. Last year, Congress authorized $2.9 billion for operating subsidies, $3.6 billion for modernization, and $0.5 billion for severely distressed public housing,

which is more modernization. That is about $5,000 for each of the 1.4 million households now living in public housing.

In addition to that, the typical family living in public housing pays about $2,000 a year as its share of operating costs. That is based on 30 percent of its income. The $5,000 in Federal subsidy and the $2,000 in tenant contribution add up to $7,000. That is just slightly more than the $6,900 that HUD now budgets for a new certificate or a new voucher each year.

These calculations compare the annual costs per unit in each program. There are differences in the budgetary treatment of public housing and housing vouchers and certificates. They would need to be addressed by the Congress and they are discussed in my statement.

My main suggestion is to adopt the new policy now, in particular, by zeroing out public housing project construction money in this year's budget. That would save $598 million. If public policy is going to be that we stop subsidized public housing projects 3 years from now, we should stop building those projects now.

Tenants in privately-owned projects would be given vouchers also, but here, there is a serious transition problem. Some of these projects may not be able to support their present mortgages if rental payments are held to fair market rent levels, to the levels of vouchers and certificates. That is a particular budget concern for the projects insured by FHA.

The blueprint and the budget propose to forestall default on these projects by marking to market the entire insured assisted housing inventory, project by project. FHA would pay part of the mortgage principal now, based on some attempt to estimate what the projects are really worth. The remaining mortgage could then be supported, in theory, by tenant voucher and certificate payments based on the fair market rent. The budget asks for $643 million to make these payments to lenders now, in 1996.

I think you should reject this proposal. It will be immensely staff intensive and immensely difficult to do well. HUD will start giving away money without any real assurance that it can avoid default and avoid insurance claims by making these payments now.

At a hearing before Mr. Shays' Oversight Subcommittee yesterday, the HUD IG expressed great skepticism about HUD's ability to run such a program. I share that skepticism. I strongly suggest that you insist on getting specific information from HUD about these projects, including such basic facts as how many projects there are in each program, how much money the mortgage amounts are on these projects, when their contracts expire, and how the current subsidies compare to the fair market rents, compare to the tenant voucher and certificate payments, before you seriously consider marking anything to market.

The way to find out what the projects are really worth is to stop subsidizing them as their contracts expire. I recognize that there may be some defaults as a result, but it will still be cheaper to let that happen than to go on providing ever more project-based subsidies in an effort to avoid paying insurance claims. HUD has been doing that for over 20 years. It hasn't been successful.

This does not require any huge immediate outlay from defaulted projects. Whatever defaults occur would be spread out over time.

Converting the present subsidies to vouchers will be a gradual process, as contracts come up for renewal over the next 15 years. Not many contracts will come up for renewal next year or in any other given year, and, therefore, not many projects are really at risk of default.

Other parts of the blueprint, unfortunately, are not consistent with the proposed reforms in low-income housing assistance. The administration wants to create a new affordable housing fund, which is the current HOME block grant, and use it as a way to build more subsidized projects at the same time it wants to stop subsidizing the projects that have already been built.

Moreover, it wants to offer FHA insurance on the new subsidized projects. We have been down this road before with section 8 new construction from 1974 to 1983, with section 236 before that, from 1968 to 1974, and with Section 221(d)(3) BMIR before that, from 1961 to 1968. Every time Congress has created a program that combines FHA multifamily insurance and subsidies to build privately owned low-income housing, you have repealed that program a few years later, often after a rash of scandals. But the projects still exist and the taxpayers are still paying on all of them.

There has been no program to fund privately owned projects since section 8 new construction was terminated in 1983. There is no reason to start one now. This is not reinventing HUD, this is back to the future.

To date, the HOME block grant has been used mainly for housing rehabilitation. It has been used for the same purposes as CDBG. HOME is budgeted at $1.4 billion this year, and CDBG at $4.9 billion. That is $6.3 billion, combined; 5 years ago, HOME didn't exist and CDBG funding was $2.9 billion.

There is no reason to have two block grants to do the same thing, no reason to spend twice as much on community development now as you spent 5 years ago, and certainly no reason to turn HOME into a production program for low-income housing. Instead of renaming HOME, I think you should terminate it, and that would save $1.4 billion.

Let me turn briefly to FHA, which is the largest part of HUD in terms of staff and commitment of Federal resources to housing, although it is not the largest part of the HUD budget. Here, I think the Reinvention Blueprint is just backwards.

FHA insures both single-family homes and multifamily projects. The single-family program works reasonably well. It helps young, middle-income families buy homes. The insurance premiums cover the claims.

The multifamily programs don't work very well. The premiums don't cover the losses at all. FHA has had to establish a $10 billion loss reserve against a $44 billion portfolio, and the budget has a 6-percent subsidy rate for multifamily insurance, on average, besides the 4-percent premium. That 6-percent subsidy translates into $188 million that must be appropriated this year.

Mortgages on multifamily projects are difficult to underwrite. Every project is unique and it has to be analyzed carefully. It takes a lot of staff. It is the same problem that FHA would face in marking to market the existing insured inventory.

FHA has about eight times as much single-family insurance in force as multifamily insurance, but FHA's staff is split 52/48 between single-family and multifamily. On top of that, I can assure you that multifamily insurance takes a vastly disproportionate share of the time and energies of HUD's top management, and even then, FHA loses money on it.

You might reinvent HUD by getting FHA out of the multifamily insurance business, leaving the basic structure of the home mortgage insurance program alone. That would be my suggestion. Eliminating multifamily insurance would save $188 million in credit reform subsidies.

This may sound drastic, but it isn't likely to have much effect on the multifamily housing market or on the availability of rental housing. In 1993, FHA insured about 5 percent of all multifamily mortgage originations, a total of $1.6 billion out of $30 billion in the whole market, and it insured about 7 percent of all new multifamily housing, 9,000 apartments out of a total of 127,000. This isn't a large volume of activity for all the headaches it causes HUD and it causes Congress.

Instead of reinventing HUD in this way, the Reinvention Blueprint does just the reverse. The multifamily program would continue unabated and unreformed, but FHA would get out of the business of insuring home mortgages, the business it actually does know how to do, and, instead, set up coinsurance schemes with private firms and State housing agencies.

The basic issue in the scheme is, who has the right to commit the full faith and credit of the Federal Government? In my view, only the Federal Government should have that right. It shouldn't be given to private entities or other levels of government which won't have to bear the cost if they make mistakes.

State agencies have always wanted the Federal Government to take all the risks in any partnership with HUD. HUD made a similar proposal last year. The House voted to limit FHA's risk exposure to 35 percent of the mortgage amount, which is close to FHA's average loss per default. The State agencies said that would destroy the program. They wanted 100 percent FHA insurance. Fortunately, Congress didn't pass either version of the program.

The blueprint also proposes to turn FHA into a government-owned, streamlined, market-driven corporation within HUD. That doesn't mean it will run any better, if it is doing the same things in the future that it has done badly in the past. The Postal Service is a government-owned corporation. It is not streamlined; it is not market driven.

For that matter, FHA itself was an independent government entity for three decades before it was part of HUD. There were scandals in FHA multifamily mortgage programs before it was part of HUD. They go back to section 608 in the late 1940's. There is no magic in this proposal to prevent scandals in the future.

To conclude, I have suggested four places where I think you can save a substantial amount of money in the HUD budget and make a difference in how HUD works. Terminate public housing construction money, and save $588 million. Terminate the HOME block grant, and save $1.4 billion. Terminate the FHA multifamily insurance, and save $188 million. Reject the administration's mark-

to-market proposal and save $643 million. That is a total of over $2.8 billion. That is 11 percent of the HUD proposed budget. It is a 9-percent reduction from this year.

If you do that, HUD would be doing the things that it knows how to do: insure FHA mortgages, give out vouchers and certificates, give whatever money you can afford for community development to States and localities in one block grant, in CDBG, without very many strings. You would get HUD out of the businesses it doesn't know how to do. That would be a reinvention of HUD that would be a real reinvention of HUD and a significant improvement on the administration's proposal.

Thank you very much.

[The prepared statement of Mr. Weicher follows:]

PREPARED STATEMENT OF DR. JOHN C. WEICHER, SENIOR FELLOW, THE HUDSON INSTITUTE

Mr. Chairman and members of the committee:

Thank you for inviting me to testify before the Budget Committee today. I am especially grateful because this year offers a historic opportunity in housing as well as in other areas of public policy, and your deliberations on the fiscal year 1996 HUD budget may be an important milestone on the path to a fundamental restructuring of HUD's activities.

I should begin by saying that, although I am a Senior Fellow at the Hudson Institute, a nonprofit policy research institution, I don't speak for the Hudson Institute or anyone else. I am here to speak only for myself, based on my experience at HUD and my professional activities. I have served at HUD in three different administrations over the last 20 years, most recently as Assistant Secretary for Policy Development and Research under President Bush and Secretary Kemp during 1989–1993. I have served on the staff of three Presidential housing commissions, two of which recommended major changes that were later enacted by Congress. I am an economist and my field of specialization is urban economics. I have devoted my professional career to the study of housing and other urban issues, since graduate school; I taught for 10 years at The Ohio State University before coming to Washington. I've written 9 books and many articles in both academic journals and the general press, and I'm working on the 10th book now.

THE BUDGET AND THE REINVENTION BLUEPRINT

The administration's fiscal year 1996 budget has been generally described as a standstill document that avoids hard choices. That is certainly true of the 1996 HUD budget. The "Reinvention Blueprint" for HUD, released last December, proposes major innovations in most program areas, but they are to be phased in over several years. The blueprint provides a better description of the strategy for HUD than does the 1996 budget. I'll therefore talk about the policy changes in the blueprint as well as the specifics of the budget. The blueprint indicates the administration's support for housing policies that were developed in the Reagan and Bush administrations, and indeed in the Nixon and Ford administrations before them. It does not go far enough in many areas—some of the proposed changes are more cosmetic than real—and it contains some bad ideas. But it certainly changes the political landscape, and offers a chance to make major changes in housing policy, particularly in the area of subsidized housing.

With one important exception, the changes proposed in the blueprint are almost nonexistent in this budget. That is because the initial stages of the blueprint merely fold a number of existing programs into block grants, without any reduction in funds, and that is about all this budget does. The real changes are scheduled to occur in 3 years: during the next administration and the next Congress.

More significant changes in the budget and in housing policy can and should be enacted now. The budget proposes $26.3 billion in both budget authority and outlays. Over $2 billion in budget authority can be saved, and at the same time HUD will be able to run its basic programs more effectively. I'll describe these savings in the context of the policy changes proposed in the Reinvention Blueprint, and summarize them at the end of my statement.

SUBSIDIZED HOUSING

The most positive proposal in the Reinvention Blueprint is a fundamental change in the structure of housing assistance for low-income families. There would be a dramatic shift from project-based assistance to tenant-based assistance—away from public housing and similar privately-owned projects, and to a system of relying on the free choices of low-income families in the private housing market. By phasing out operating subsidies and modernization funding for public housing and converting the money to housing vouchers for the residents, the blueprint would force PHA's to compete with private landlords for tenants. It would take away their guaranteed, captive, tenants, and subject them to the discipline of the housing market. The same policy would apply to private projects—section 8 new construction and its predecessors—as their current contracts with HUD expire. And all future incremental assistance would take the form of vouchers or certificates.

This could prove to be the final stage in a policy evolution that began in 1970, afler a recommendation by the Kaiser Commission to give housing allowances directly to poor families. It is a logical development. Since at least the 1950's, we as a society have not been happy with public housing, and have recognized that the living environment in many projects is "worse than the slums they replaced," as the urban critic Jane Jacobs wrote in 1961. In reaction, successive Congresses and administrations have enacted a series of programs to build subsidized private low-income projects, and then repealed them a few years later: Section 221(d)(3) (BMIR), created in 1961, repealed in 1968; section 236, created in 1968, repealed in 1974; section 8 new construction, created in 1974, repealed in 1983. We have never been satisfied either with the cost or the quality of the housing produced in these programs, and so they are terminated and replaced. This is very rare for any government agency.

Meanwhile, incremental housing assistance has increasingly taken the form of vouchers and certificates. Over 1.1 million families and elderly individuals now receive housing vouchers or certificates, and most incremental assistance has taken the form of vouchers or certificates over the last 15 years. Vouchers and certificates work for all kinds of families, in all kinds of markets. On a scale of 1 to 10, two-thirds of the recipients rate their housing at 8 or better. This is true for African-American and Hispanic families as well as for whites. Over half of voucher and certificate recipients are African-American or Hispanic.

While the voucher and certificate programs work well now, they can be improved by legislative changes. In particular, private landlords should be relieved of the 1992 legislative restriction that if they take one voucher or certificate recipient, they have to take any who apply; they should be allowed to choose how many and which voucher recipients they want to have as tenants—subject to the Fair Housing Act and other laws governing discrimination. This is something that HUD proposed last year.

This committee will be especially interested to know that project-based assistance can be turned into vouchers and certificates at no additional cost, and indeed at some savings. The costs of operating and modernizing public housing have grown greatly over the years. In 1995 Congress authorized $2.9 billion for operating subsidies, $3.6 billion for modernization, and $0.5 billion for "severely distressed" public housing. There are about 1.4 million households living in public housing. Per household, that is about $5,000. In 1989, which is the most recent published data, the typical family living in public housing had an income of about $6,500. It is expected to pay 30 percent of its income—about $2,000—as the tenant share of operating costs. The $5,000 in operating and modernization subsidies and the $2,000 in tenant contribution add up to about as much as the $6,900 that HUD now budgets for an incremental housing certificate each year. That is, if each family living in public housing received the $5,000 HUD is now spending on operating subsidies and modernization, and continued to spend 30 percent of its own income on rent, it could afford anything renting at or below the Fair Market Rent on the private market.

These calculations compare the annual costs per unit in each program. There are differences in the budgetary treatment of public housing on the one hand, and vouchers and certificates on the other, that will need to be addressed by the Congress. Operating subsidies and modernization are authorized 1 year at a time, while vouchers and certificates carry multiple-year authority, typically 5 years. Also, the authorization for operating subsidies takes account of the tenant's income and covers the difference between the tenant's rent payment and total operating costs, while the authorization for vouchers and certificates takes no account of the tenant's income, and assumes that the government will pay the full rent of the apartment.

If public housing residents want to use their vouchers to move, they will be able to find decent housing that they can afford in the private market, if they want to.

The supply of available decent housing renting for the FMR or less is large enough to accommodate current residents of public housing even if all of them choose to move.

There is, however, no reason to expect that most public housing residents will choose to move. The elderly, in particular, are likely to want to stay in their present apartments. Most PHA's do a reasonably good job of providing housing. But most of the large PHA's don't do as well; many have been officially and deservedly designated as "troubled" by HUD. In many cities there are one or two projects that are notorious locally as terrible places to live and raise a family. All of the residents, satisfied or not, will benefit if PHA's and project owners have to earn the tenant's dollars.

The problem with this proposal is that, according to the Reinvention Blueprint, these desirable changes are not scheduled to happen for 3 years. The only thing that happens in the fiscal year 1996 budget is that various public housing programs are consolidated into two block grants: one for operations and one for capital outlays, including both modernization and construction of new projects. All the money appropriated for these programs in 1995 would be folded into the two new block grants, with no savings.

The Congress may want to expedite that schedule. If vouchering out public housing is a good idea, the time to start doing it is now, not 3 years from now. Instead of creating two new block grants, Congress should convert operating subsidies and modernization into vouchers and certificates. The danger is that 3 years will pass without serious HUD efforts to work out the details.

As part of vouchering out, public housing project development should be zeroed out in this year's budget. It costs $85,000 to build each new public housing unit. That would save $598 million. This should be done whether vouchering out starts now or after a transition period. There is no reason to build more subsidized projects now, if it is the policy decision to stop subsidizing them as projects 2 years from now.

The longer Congress lets the administration wait to change the policy, the more public housing costs are likely to rise. In 1980, operating subsidies were $0.9 billion—they were being blamed on the oil embargo—and $0.5 billion worth of modernization was financed. Even allowing for inflation, budget authority and outlays in 1995 were more than double budget authority and outlays in 1980. Modernization sometimes seems to be a bottomless pit. Every few years there is a new study of modernization needs, and Congress raises the annual appropriation in response; then a few years later there is another study, and it turns out that total modernization needs are higher than they were in the previous study, even after spending several billion dollars. If Congress creates a new public housing capital block grant as a transition mechanism, the process is likely to be repeated.

PRIVATELY OWNED FHA-INSURED PROJECTS

The Reinvention Blueprint proposes to apply the same concept of vouchering out to privately-owned projects, though on a slower timetable and with transition practices that are likely to be counterproductive and costly. Tenants have incomes about 15 percent higher on average than public housing tenants, so it is certainly possible that these projects too can be vouchered out; tenants can use the current project-based subsidies to find housing they can afford in the private market, if they want to move. As in the case of public housing, it is not likely that many will choose to move. Some 40 percent of the households in these projects are elderly, and appear to be very satisfied.

There is an important question of what happens to the projects. Detailed information about the costs of operating the privately owned projects is not regularly published in the HUD budget, but under the Low-Income Housing Preservation and Resident Homeownership Act (LIHPRHA), costs can be above the FMR when contracts are renegotiated. Many carry mortgages based on tenant payments in excess of the FMR's. The budget proposes legislative changes in LIHPRHA to bring the maximum subsidies down to the FMR; at present it is 120 percent of the FMR. Bringing subsidies back in line with market rents is all to the good.

Some projects may not be able to support their present mortgages if rental payments are held to FMR's. That's a particular concern for the projects insured by FHA. The blueprint and the budget propose to forestall defaults by "marking to market" the entire insured assisted housing inventory, project by project. (The budget says that marking to market will be applied to the older insured inventory, which is about two-thirds of the total; it's not clear whether the rest of the inventory would be marked to market later, or whether the administration is changing its proposal.) Under marking to market, FHA would pay part of the mortgage principal now,

based on some attempt to estimate what the projects are really worth. The remaining mortgage could then be supported, in theory, by tenant voucher and certificate payments based on the FMR's. The budget asks for $643 million to make these payments to lenders in 1996.

This proposal should be rejected. It will be immensely staff-intensive and immensely difficult to do well. HUD will start giving away money without any real assurance that it can avoid default and insurance claims by doing so.

The way to find out what these projects are really worth is to stop subsidizing them. Financial incentives to preserve them should be discontinued. If the projects are going to have to compete with other privately owned housing for tenants, that competition should start as soon as possible. Unlike the process of vouchering out public housing, this will be gradual, as contracts and commitments expire or come up for renewal. Most projects now have ongoing commitments from the Federal Government; relatively few of those commitments will expire this year, or in any other particular year.

I recognize that some privately owned projects may go into default without the project-based commitment. Where the projects carry FHA insurance, that will cost the government money. It will still be cheaper to let that happen than to go on providing project-based subsidies, one on top of the other, in an effort to stave off default and avoid paying an insurance claim. "Marking to market" is in essence the latest version of "flexibile subsidy"—putting money into projects where the rents can't support the mortgage and operating costs, trying to avoid defaults. The sorry history of these efforts can be traced in HUD budgets over the past two decades.

Moreover, these programs invite abuse. Scandals are more likely to occur where subsidies are piled on top of each other. It is hard to limit the subsidies to exactly the amount that is needed to keep the project operating and not give the owners a windfall profit. This is where consultants and influence peddlers have been especially active, as in the section 8 mod rehab program a few years ago.

Allowing projects to go into default, if tenants don't want to live in them, also shows that HUD is serious about tenant-based assistance. Other project owners will take notice, and perhaps take action to avoid default. This point should not be overemphasized, but it is a good idea not to leave project owners with the idea that they will always be bailed out by the Federal Government, no matter how badly they run their projects.

As with the proposal to voucher out public housing, there are problems in the transition. It is slow, and the transition procedures are counterproductive and costly. Preservation incentives, at the reduced scale, would be extended to additional projects during a 3-year transition period, resulting in further long-term commitments for project-based assistance. Again, the time to start is now, not 3 years from now.

A LOW-INCOME HOUSING BLOCK GRANT?

There have been some suggestions that low-income housing assistance should be turned into a block grant, as part of welfare reform, and the Reinvention Blueprint refers to consolidating housing assistance programs into a "performance-based fund," alongside the HOME and CDBG block grants. The welfare system certainly needs reform, as soon as possible. Turning the voucher and certificate programs into a block grant, however, is not necessary to that effort, and may not be helpful. The programs are basically efficient and effective as they are now operated, in all kinds of housing markets across the country. Incremental assistance is now allocated to the smallest geographic areas that are practicable, on the basis of a legislative formula representing the need for assistance among the residents of different jurisdictions. That is close to a block grant as an allocating mechanism. In addition, as I mentioned earlier, the government now makes commitments for assistance to recipients for a term of years. Outlays under those commitments would continue under the present system, while new commitments would be made under the block grant, which is likely to be administratively cumbersome for both HUD and the state and local government agencies that operate the programs.

THE AFFORDABLE HOUSING FUND

Unfortunately, other proposed changes are fundamentally inconsistent with the reforms in low-income housing assistance. The Affordable Housing Fund (the current HOME block grant) is intended to be a production vehicle for more new low-income housing projects at the same time that the projects we now have are being vouchered out. It is not clear why there is a need for a new program of building low-income projects, when we appear to have bipartisan consensus that the concept itself is flawed and certainly is inferior to the voucher program. Moreover, the blue-

print is silent as to how the prospective tenants are expected to afford to rent apartments in these new projects, because project-based subsidies are being terminated.

Worst of all, the reinvention blueprint also envisions combining Affordable Housing Fund money with FHA insurance on the projects that cities or states finance with that money. This is a proven recipe for disaster. The worst HUD scandals and management problems have occurred in subsidized projects that HUD insures. There is always pressure to underwrite them generously, "in a good cause." Once they are insured, there is an effort to avoid foreclosure on the projects, if the project-based subsidies aren't enough to support them, or the landlords can't manage them efficiently. Foreclosing on the project would be admitting failure, being unable to underwrite properly. HUD would have to take over the management of the project, which it is loath to do. The alternative is to provide additional subsidies. HUD's role as insurer therefore forces it into a role as continuing provider of subsidies. The insurance also makes it hard for HUD to enforce the contractual responsibilities of the landlords, because the landlords always have the option of defaulting and forcing HUD to take over the project. Ultimately HUD's role as insurer makes it the slumlord of last resort for the worst projects.

If the Reinvention Blueprint is adopted, this process will continue. There will be pressure to create new project-based subsidy programs to bail out the projects. In a few years, Congress would be considering new versions of Flexible Subsidy and its predecessors going back to the "troubled projects" program of the 1970's. The opportunity to make fundamental reforms in housing programs and housing policy would be lost.

Instead of being renamed, HOME should be terminated. That would save $1.4 billion. To date, HOME has primarily been used for housing rehabilitation, much like CDBG. HOME was created in 1990; at that time CDBG funding was $2.9 billion. In this year's budget, they amount to $6.3 billion combined. There is no reason to have two block grants to do the same thing, no reason to spend twice as much on community development now as 5 years ago, and no reason to turn HOME into a production program.

BLOCK GRANTS AND PROGRAM CONSOLIDATION

The administration proposes to consolidate a number of smaller existing programs into the two major block grants, CDBG and HOME. Consolidation is generally a good idea; it permits reductions in agency staff and lets local officials make their own decisions about what should be done. CDBG and HOME amount to about 85 percent of the funds appropriated for the programs of the Office of Community Planning and Development at HUD, but only about 75 percent of the field office program staff, and probably about half of the central office program staff. The various special needs housing programs that would be consolidated into HOME could be consolidated into CDBG instead. The same savings in staff at the Federal level could be realized, and so could any improvements in program efficiency at the state and local levels.

At the same time, it is worth noting that some of the programs that would be consolidated into the block grants now provide funds directly to nonprofit organizations to help the homeless and other groups. There is some sleight-of-hand in the administration's budget presentation, purporting to show that states and cities will get more money—a rather disingenuous claim that is true only because these program funds would go instead to states and cities. There is no reason to believe that the states and cities will administer the programs more effectively than the nonprofits are doing now, and they may need more staff if they plan to continue them with block grant funds.

THE FEDERAL HOUSING ADMINISTRATION

With respect to FHA, which is the largest part of HUD in terms of staff and commitment of Federal resources to housing, the Reinvention Blueprint is just backwards. FHA consists of single-family home insurance—section 203—and a variety of multifamily insurance programs. The single-family insurance program works reasonably well. It helps young, middle-income families buy homes and the insurance premiums cover the costs of foreclosure and claims. The Mutual Mortgage Insurance Fund has a positive net worth.

The multifamily programs don't work very well. The insurance premiums do not cover the costs, and they require annual appropriations for the losses. FHA has had to establish a $10 billion loss reserve against a portfolio of $44 billion. The losses are continuing: the 1995 budget included a 6 percent subsidy rate for multifamily insurance on average, meaning that losses will be 6 cents on every dollar of additional multifamily insurance—in addition to the 4 cent insurance premium. The

credit subsidy in the fiscal year 1996 budget is $188 million. Losses are projected to range from 2 cents to 30 cents, in various programs. (A few programs are expected to cover their losses out of premiums.)

Mortgages on multifamily projects are difficult to underwrite and insure, and not just for FHA. Freddie Mac lost money on its multifamily mortgage purchases in the late 1980's and early 1990's and discontinued its multifamily programs for several years. Every project is unique and has to be analyzed carefully, which is very staff-intensive. This is the same problem with the "mark-to-market" approach for existing projects. It's very difficult to underwrite multifamily projects in the first place, and very difficult to re-underwrite them after they are built. HUD has about eight times as much single-family insurance in force as multifamily insurance. However, HUD's staff is split about 52–48 between single-family and multifamily. Multifamily insurance takes a vastly disproportionate share of staff time and resources, including the central management of the department, and it still costs the taxpayers a lot of money. The complicated nature of multifamily projects is a basic reason for all the scandals.

One might "reinvent HUD" by getting FHA out of the multifamily mortgage insurance business, leaving the basic structure of the home mortgage insurance program alone. Eliminating multifamily insurance would save the $188 million in credit reform subsidies. This may sound radical, but it is not likely to have much effect on multifamily housing production or financing, or on the availability of rental housing. In 1993, the last full year for which data are available, FHA insured about 5 percent of all multifamily mortgage originations—$1.6 billion out of $30 billion. It also insured about 7 percent of all new multifamily housing—9,000 out of 127,000 apartments. This is not a large volume of activity to be worth all the headaches it causes HUD.

Under the Reinvention Blueprint, however, the multifamily mortgage program would continue unabated. But FHA would begin to get out of the business of insuring home mortgages, which it knows how to do, and instead launch joint insurance schemes with private firms and state housing agencies.

Joint insurance is a fine way to lose money, as FHA has demonstrated in the past. In the 1 980's it created a similar multifamily coinsurance program for mortgages on rental properties. HUD shared insurance premiums and risks with private lenders, letting the lenders do the underwriting. When defaults occurred, it turned out that the lenders had no capital to meet their share of the losses, and HUD wound up taking the full loss. This has been one of its costliest failures ever.

State housing agencies have more capital than the private lenders did, but splitting the risk is still an issue for them. The agencies have always wanted the Federal Government to take the full risk in any partnership with HUD. When HUD made a similar proposal in last year's housing bill, the House of Representatives wanted to limit FHA's risk exposure on each mortgage to 35 percent of the original amount borrowed, which is close to FHA's average loss on a defaulted mortgage, but the state agencies said the 35 percent limitation would "destroy the program." Fortunately, Congress didn't pass either version of it.

Last year's experience brings out the basic issue in these schemes: Who has the right to commit the full credit of the Federal Government? In my view, that commitment should remain a responsibility of the Federal Government, and not be given to private entities or other levels of government which will not have to bear the costs if they make mistakes. Even if some degree of risk sharing is legislated, large units of government can still go bankrupt, as Orange County is now demonstrating, and nobody's pockets are as deep as the Federal Government's. Moreover, virtually all FHA mortgages are sold to investors in the form of securities issued by the Government National Mortgage Association, which guarantees the timely payment of principal and interest even if the homeowner defaults, and therefore has to make up for any delay on the part of the nonfederal participant in meeting its obligations. GNMA and FHA had to make good the losses in the multifamily coinsurance program.

The likely outcome of these joint insurance schemes is that HUD would continue to bear all the cost of the program, but with less premium income. The losses would not show up in this year's budget, but the lower premium income would. If the capital markets conclude that joint insurance dilutes the value of the Federal guarantee, homebuyers would pay higher mortgage rates as well.

FHA insurance could and should be better targeted to lower-income families, say those in the bottom half of the income distribution; as things now stand, families with incomes of $80,000 a year are eligible for government-supported mortgage insurance in some parts of the country. That is a long way from the original clientele of young moderate-income families buying their first home. But for those young

moderate-income families, FHA insurance serves a market that private insurers have so far not reached, and FHA serves it without losing money.

REORGANIZATION

Although the subject of reorganizing HUD is not central to the immediate jurisdiction of this committee, it may be useful to offer some comments on the Reinvention Blueprint proposals in this regard, and other options as well.

The blueprint proposes to turn FHA into a "government-owned, streamlined, market-driven" corporation within HUD. That doesn't mean it will run any better, if it is doing the same things in the future that it has done badly in the past. The Postal Service is a government-owned corporation. It is neither streamlined nor market-driven.

For that matter, FHA was an independent government agency for three decades. There were scandals in the multifamily mortgage insurance programs of FHA before it was part of HUD, going back to section 608 in the 1940's, and problems with programs combining FHA insurance and project-based subsidies, such as Section 221(d)(3) BMIR in the 1960's. There's no magic in this proposed reorganization to prevent scandals in the future.

Another suggestion is to privatize FHA. This is tempting, but not finally desirable on policy or administrative grounds. If the government still intends to promote home ownership, FHA has a unique role. It serves families with lower incomes and less ability to make a downpayment than the private mortgage insurance industry has so far been able to serve. FHA should not be protected from the PMI's; it should have to compete with them. It has been losing market share to the PMI's most of the time since the 1950's, and ultimately the PMI's may be able to serve the entire market, but that time does not yet seem to have arrived.

CONCLUSION

In this testimony I have recommended four areas where HUD's budget could be cut and program operations could be reformed at the same time.

(1) Discontinue public housing development money: $598 million.

(2) Terminate the HOME block grant: $1.400 billion.

(3) End FHA insurance of multifamily projects: $188 million.

(4) Reject the "mark-to-market" concept for the insured assisted inventory: $643 million.

Together these savings add up to $2.829 billion. That's 11 percent of the administration's proposed fiscal year 1996 HUD budget. Budget authority would be 9 percent less than the fiscal year 1995 level.

There would be additional savings if the FHA single-family home mortgage insurance is left alone, since premium income would not be shared with private firms or state agencies. There would also be savings in salaries and expenses from terminating HOME and FHA multifamily insurance. I haven't tried to quantify these savings.

These budget savings would also constitute a true reinvention of HUD. HUD would continue to do the things it can do, and that serve a public policy purpose: insuring single-family mortgages (and securitizing them through GNMA), giving vouchers to low-income families so they can afford decent housing that they want to live in, and giving state and local government whatever funds it can afford for community development in one block grant, with few or no strings. These things can be and are being done reasonably well at HUD.

At the same time, HUD would stop doing the things it has not done well for several decades. It would stop insuring multifamily mortgages, stop subsidizing the construction of low-income housing projects (either directly or through a block grant), and above all stay out of the business of combining multifamily insurance with project-based subsidies.

That would be a much more significant reform of HUD than the administration's Reinvention Blueprint.

Chairman KASICH. Thank you. That was very enlightening. Dr. Utt.

STATEMENT OF DR. RONALD D. UTT, VISITING FELLOW, THE HERITAGE FOUNDATION

Mr. UTT. Thank you. Mr. Chairman, members of the Budget Committee, thank you for inviting me to be here today to present

my views on President Clinton's fiscal year 1996 HUD budget proposal and also to discuss possible alternative directions that housing policy might take in the future to better serve those in need.

Let me begin by saying that the views I express today are mine and mine alone and do not reflect those of the Heritage Foundation, where I am now a visiting fellow.

In the interest of time, my remarks here today are summarized from a somewhat lengthier statement that I have already submitted to the committee, and I request that it be included in the record.

By way of introduction, my background in the housing area is a rather eclectic one, beginning originally at HUD in the early 1970's, where I was part of a team brought in from around the country in the wake of a series of costly failures and scandals.

Subsequently, I worked on related housing and real estate policy issues at the Office of Management and Budget, and later with several real estate and business trade associations, as well as think tanks. Most recently, I have been a direct participant in the housing market as a licensed general contractor specializing in the acquisition, renovation, and resale of residential housing.

I would like to begin my statement this morning by commending Secretary Cisneros for a program that, at least in spirit, represents a major break with the patterns and practices of the past and which proposes to redirect HUD resources in more productive ways, chiefly by favoring household-based assistance over the more costly project-based assistance.

Also high on the list is the proposal for an orderly withdrawal of direct Federal support for public housing and the proposal to provide the existing residents of public housing with the resources necessary to exercise their choice in housing.

Less attractive are the proposals for a new affordable housing fund, which would perpetuate, under different names, the more costly project-based assistance of the past, and the new entrepreneurial FHA, which appears to steer FHA away from what I believe is its most valuable mission and toward a whole host of new, potentially risky missions and partnerships.

Also troubling, and I concur with John on this, is the extended timeframe in which the above reforms are projected to occur. As I read the blueprint that came out in the middle of December, there was very little correspondence between that document and the budgetary numbers that were ultimately sent up. As I see it, the directions for at least 1996 and 1997 are not altogether different than the directions set in the past.

Several years ago, in a different time, the successful implementation of the primary proposals introduced by Secretary Cisneros would have marked a significant and positive change for HUD policies. But times change, new opportunities emerge, and I believe that the resources now controlled by HUD could be more effectively used if they were combined into a social welfare block grant to the States, with the Governors and mayors authorized to determine the extent to which these resources are used for housing, direct income assistance, child care, job placement, and other opportunities, within the context of a series of guidelines designed to move low-income households from long-term dependency to self-sufficiency.

At present and with most of its resources targeted to households with low to moderate incomes, HUD is an integral part of the U.S. welfare system, and, as such, should be an integral part of any solution, one that contains powerful incentives to self-sufficiency rather than the costly, dependency-creating, custodial function that the system, including HUD, performs today.

My colleagues at the Heritage Foundation have had a long involvement in developing effective welfare reform plans, and, very briefly, the key components of that plan include controlling costs and providing State flexibility, establishing sensible and workable workfare, and reducing illegitimacy.

Included in this block grant would be the funds representing approximately 80 percent of HUD's budget, which now go toward a variety of means-tested housing assistance programs, including public housing, section 8 new construction and renovation, as well as section 8 vouchers and certificates, the old section 236 program, and other remnants of past subsidy programs.

I recommend that the low-income housing assistance funds targeted to these programs be combined into a single welfare block grant to the States to be used at the discretion of Governors and mayors under general guidelines established by Congress. Governors would have some measure of flexibility in allocating the block grant among a variety of objectives, as discussed above, according to where the need is greatest within each community.

To the greatest extent possible, what direct housing assistance has provided should be provided through household-based arrangements, rather than project-based programs, except in special cases, such as housing assistance for the elderly and disabled, and, also, where costs and quality of life are competitive with that provided by the way of vouchers.

Such a proposal is not as extreme as it would appear, relative to current arrangements. At present, much of HUD's housing assistance, including the many forms of assistance to public housing as well as section 8 voucher and certificates, are provided to eligible beneficiaries by way of local housing authorities who, under my proposal, would now be acting on behalf of their Governor, rather than HUD.

In this regard, most of the remaining 20 percent of HUD's budget is for community development block grant programs, which would be made redundant by the welfare block grant proposed above and, thus, should be terminated.

Of the two remaining major programmatic areas, I recommend that FHA be converted into a financially self-sufficient, independent government corporation, with responsibility for assisting creditworthy households of moderate incomes to acquire their own homes on an unsubsidized basis that does not jeopardize the financial health of the insurance fund.

Finally, HUD's role in ensuring that fair housing laws be met should be transferred to the Civil Rights Division of the Justice Department, which also has been active in investigating and rectifying housing and mortgage lending discrimination.

On a concluding note, it should be recognized that any major changes in programs, such as those that operate at HUD, must take into consideration the extensive array of long-term financial

commitments that HUD has made to a variety of private and public entities that provide different types of housing assistance to eligible households. Cost-effective mechanisms consistent with the overall goal of comprehensive welfare reform must be implemented to ensure the orderly transition from one type of housing assistance to another.

That concludes my oral statement. I would be pleased to respond to your questions.

[The prepared statement of Mr. Utt follows:]

PREPARED STATEMENT OF DR. RONALD D. UTT, VISITING FELLOW, THE HERITAGE FOUNDATION

INTRODUCTION

In response to the last election, the members of the new Congress and the President and his cabinet have indicated a predilection toward a radical overhaul of the Federal Government and its hundreds of costly programs. Among the chief targets of this prospective restructuring is the Department of Housing and Urban Development (HUD), whose very existence is being questioned by both the Congress and the executive.

Such a questioning is most appropriate, and a strong case can be made for its dissolution for reasons far more important than any near term budgetary savings or deficit reduction targets. With the vast majority of its programs focused on low- to moderate-income households, HUD is an integral part of the nation's failed welfare system. For this reason any changes made to HUD must be consistent with the welfare reform goals of ending long-term dependency and creating strong incentives for self-sufficiency.

Of the many possible directions that welfare reform could take, the one now favored by a significant number of House and Senate members is to shift the welfare responsibility and the necessary financial resources to the states in the form of block grants. The housing assistance responsibilities and resources that now belong to HUD and comprise about 80 percent of its budget, should be part of these block grants, and the other programs operated by HUD should be terminated, transferred or privatized, as discussed later in this statement.

Created in 1965 out of several existing government entities involved in housing, mortgage finance, and urban issues, the creation of HUD was the Federal Government's response to the emerging urban crisis that had manifested itself in a series of destructive and deadly inner city riots. The concern then, as it is today, was the emergence of an impoverished urban underclass subject to low educational attainment, family dissolution, unemployment, high crime, poor health, and inadequate housing.

As the unfortunate record indicates, and despite the spending of more than $5 trillion in means-tested assistance by HUD and other Departments since 1965, our urban problems are worse and the number of low-income, non-elderly households is not materially different today than it was back then, although the environments in which many live are far more dangerous and despairing.

HUD, however, is just one of many weapons brought to the battle by the Federal Government, which in the years since has marshaled the resources and attention of most of its domestic departments in the fight against poverty and the ills of the declining cities. Along with HUD, the Departments of Agriculture, Health and Human Services, Labor, Education and Justice provide food stamps, Medicaid, Aid to Families with Dependent Children, education and law enforcement grants, job training and a host of other programs. In fiscal year 1993, the most recent year in which complete estimates can be made, such means-tested spending amounted to a staggering $324 billion dollars, of which a little under $30 billion was for housing aid, and urban and community development programs, mostly operated through HUD.[1]

HOUSING REFORM AS A COMPONENT OF WELFARE REFORM

The welfare system we have created is costly and administratively intensive at all layers of government. Rather than directly addressing the chief problem—inadequate incomes and their cause—with an administratively simple solution—cash

[1] "The Scope of the Welfare State," by Robert Rector, the Heritage Foundation, testimony before the Committee on Government Affairs, U.S. Senate, January 25, 1995, pp. 2–3.

grants along with strong incentives to become productively employed and to take full responsibility for one's life and family, we instead choose to focus mostly on symptoms—poor diet, poor health and poor housing—and have, in turn, created a costly administrative infrastructure, particularly with regard to housing assistance, that bureaucratically attempts to address each: Food stamps to improve your diet, Medicaid to improve your health, and dozens of HUD programs to improve your housing.

Although the focus of this paper is on HUD and its housing programs, any fundamental reform of the housing assistance programs must be accomplished within the context of overall reform of the Federal welfare system, and that the key components of that reform must include strong incentives for self sufficiency, consumer choice, administrative efficiency and work requirements for able-bodied, non-elderly recipients.[2] At present, with its emphasis on project-based assistance which collects the needy in government-subsidized and government-run housing projects, the housing component of our welfare system largely fulfills a custodial function, often segregating the poor in out of the way places with high crime and few job opportunities. What is needed instead is a system that diminishes the number of poor, and HUD, whose programs are largely targeted to low-income households and communities, must be a part of this new system.

Although there is some overlap, HUD's programs operate in four main functional areas covering (1) Low Income Housing Assistance, (2) Community Development Block Grants, (3) Mortgage Insurance (the FHA and GNMA) and (4) Fair Housing. The low-income housing assistance programs are HUD's largest functional area and absorb about 80 percent of HUD's budget through a variety of different programs. Most of the remaining 20 percent is in the Community Development Block Grant program, which is primarily oriented toward housing-related initiatives rather than non-housing infrastructure projects such as parks, commercial redevelopment, etc. The single family mortgage insurance functions have generally been self-financing over the long-term, while the budget for Fair Housing activities is just a small fraction of the first two.

In recognition that much of HUD's programs are already operated through state and local housing authorities under HUD's guidance and directives, this paper proposes to merge all low-income housing assistance programs into a single welfare block grant for the states, and that the states be encouraged to administer that portion of the grant they allocate to housing assistance (except for special cases discussed later) in the form of housing vouchers and certificates that permit the eligible households to choose where they want to live. At the same time, procedures would be established for the orderly withdrawal of all direct Federal support for public housing and other forms of costly project-based assistance. How such a withdrawal could be conducted is discussed later in the paper.

The low-income housing assistance programs that would be consolidated into the housing block grant, account for approximately 80 percent of HUD's current budget. The Community Development Block Grant program accounts for most of the rest of HUD's budget, and by law must target 70 percent of its spending to needier communities. The grants, which mostly are used for a variety of housing purposes, would be made redundant by the above-proposed housing block grant program and thus should be eliminated.

The single family mortgage insurance programs of the Federal Housing Administration (FHA), would be reorganized into an independent government corporation while its portfolio was cleaned up in preparation for eventual privatization. Much of the FHA's recent financial difficulties have been largely due to costly defaults and foreclosures of FHA insured mortgages on the subsidized, multifamily housing projects.

Finally, HUD's Office of Fair Housing, whose chief purpose should be to prevent housing discrimination, would be transferred to the civil rights division of the Justice Department where the issue can be more effectively and efficiently pursued in the context of overall civil rights enforcement.

By establishing block grants and encouraging that the funds provided be utilized primarily for household-based assistance, rather than the project-based assistance that now dominates the HUD programs and are twice as costly per household served, the government would be able to provide higher quality assistance to more people at less cost. At the same time, by linking the housing assistance to overall welfare reform, we can begin the process of moving people to self-sufficiency and

[2] "Four Themes of Welfare Reform," by Robert Rector, the Heritage Foundation, testimony before the Committee on Economic and Educational Opportunities, U.S. House of Representatives, January 18, 1995.

ending the long-term dependency that has come to characterize many of these programs.

REFORMING THE GOVERNMENT'S INVOLVEMENT IN HOUSING: ADDITIONAL DETAILS

Low-Income Housing Assistance. Since the early seventies much of the debate over housing policy has been between the advocates of project-based assistance versus those who favor household-based assistance. Arguing that an individual's apparent housing problems—defined as substandard housing, overcrowding, high rent payments to income, etc.—are in fact income problems, advocates of household-based assistance propose to improve housing conditions by providing eligible households with the financial wherewithal to acquire better housing. While a cash payment would be the most efficient way of rectifying the problem, in practice the assisted household is given a cash equivalent in the form of a voucher or certificate that can be used to pay the rent or some portion thereof in suitable apartments provided by private sector landlords or other entities.

As such, a housing voucher program largely conforms to the process and purpose of most other government assistance programs such as food stamps, student loans, Medicare and Medicaid, and unemployment compensation. In each of these programs, government provides the eligible individual with the means to acquire the product or service, but the actual product or service is generally provided by the private sector, nonprofit institutions or state and local governments.

The alternative to household-based assistance is project-based assistance where the government subsidizes through a variety of mechanisms the construction, renovation, acquisition and/or operation of multifamily housing projects where some or all of the units are reserved for occupancy by low-income households. At present, approximately 70 percent of those who are assisted through HUD program's are in the project-based programs, while the other 30 percent are in household-based programs such as vouchers and certificates.[3]

The advantages of a household-based program over those that are project-based are chiefly of two types. First, household-based assistance is about half the cost of project-based financing.[4] The table below, which was compiled by the Office of Management and Budget for President Reagan's Commission on Privatization, provides the 20-year costs per household assisted for several of the major housing programs. The first two are household-based, while the next four are project-based, and include an Agriculture Department program for qualified residents of rural areas.

Program	*20-year cost*
Voucher	$27,892
Section 8 Certificate	27,955
Farmer's Home Section 515	35,210
Rental Housing Development Grant	53,500
Section 8/292 Housing	53,575
Public Housing	69,863

Source: Report of the President's Commission on Privatization, Table 3, p. 11.

Inasmuch as HUD housing assistance programs are not entitlements, but operate on a first-come first-served basis which leaves many eligible low-income households unassisted, any reform that improves program efficiency also increases the number of beneficiaries for the same total costs, or less.[5]

The second major benefit is that the vouchers are portable and allow the recipient a measure of choice in finding suitable housing to rent. In this way, assisted households can integrate themselves in the community at large according to their own interests and needs, permitting, for example, a family with young children to make neighborhood choices with regard to schools, or an elderly individual choices with regard to family and friends.[6] In contrast, project-based assistance concentrates the

[3] "The Challenges Facing Federal Rental Assistance Programs," a CBO study, the Congressional Budget Office, December 1994, p. xiii.

[4] "Privatization: Toward More Effective Government," Report of the President's Commission on Privatization, March 1988, p. 11.

[5] CBO study, p. xiii.

[6] While many see this outcome as an advantage of vouchers, this view is not universal among housing analysts. In the January/February 1995 issue of The New Democrat, Howard Husock of the John F. Kennedy School of Government at Harvard University writes that "Rent subsidies, which now go to more than 1 million households, aim at dispersing poor families rather than concentrating them. In practice, this has often meant injecting the problems of public housing into previously stable neighborhoods."

assisted, and thus largely the poor, in segregated settings that often are unsafe and distant from job opportunities and good schools. According to a recent CBO study: "* * * the evidence presented in this analysis suggests that with the exception of the elderly, recipients of household-based aid are less likely than recipients of project-based aid to be dissatisfied with their housing units or the condition of their neighborhoods. That pattern is apparent even though the incidence of substandard or crowded units is roughly the same for both types of aid among households of the same type."[7]

Efforts to integrate project-based assistance into better parts of the community usually meet with intense community resistance out of fear that such a large number of poor concentrated in one or two buildings would destabilize the neighborhood.

These benefits have not been lost on officials at HUD, and previous Secretaries from both parties have attempted to shift resources from the project-based programs to those that are household-based for all of the reasons cited above. Unfortunately, past Congresses, often influenced by special interests in the housing industry and within the local public housing authorities, have been successful in directing the bulk of HUD spending toward costly and inefficient subsidized housing projects.

Last year's Senate appropriations bill is illustrative of this point.[8] It allocates $598 million to public housing development, $300 million to Indian housing, $3.8 billion to the renovation and modernization of public housing, $1.7 billion to project-based housing for the elderly and disabled, $250 million for preservation, $555 million in property disposition costs, $500 million in the project-based Neighborhood LIFT program, $3.7 billion in expiring section 8 contracts (a majority of which are project-based), $2.9 billion in public housing operating subsidies, $500 million for severely distressed public housing, $350 million in grants to eliminate drugs from public housing, and $1.5 billion for the HOME Investment Partnerships Program, also largely a project-based program.

What is available for household-based assistance is a fraction of this, largely comprised of the $2.1 billion for incremental housing assistance, and some minor portion of the $3.7 billion for expiring section 8 contracts. It should also be noted that in virtually all cases, the Senate increased funding for all of Secretary Cisneros' proposed project-based programs, and decreased funding for all of his proposed household-based initiatives.

In his December 19, 1994, Reinvention Blueprint, Secretary Cisneros' goes much further than in previous years and proposes that (1) the bulk of HUD housing assistance be shifted to household-based programs, that (2) the current occupants of public housing be given vouchers that would allow them to leave the projects if they wished, thereby forcing local public housing authorities to compete for tenants, and that (3) a process for the orderly withdrawal of all Federal support for public housing be established.

Though he also proposed the continuation of a project-based program called the Affordable Housing Fund, which is similar to the project-based HOME program, and a new, entrepreneurial FHA, the ideal behind Secretary Cisneros' program is a positive change from the past and should be endorsed by this Congress, albeit only in spirit.

Congress should build on this effort and move the concept another step further by combining all low-income housing assistance funds in a welfare block grant to the states and encourage them to apply the funds they allocate for housing toward household-based assistance, except for those special cases where project-based programs best serve the assisted's needs, or where projects are well-managed and efficiently run at per household costs comparable to those associated with vouchers.

Community Development Block Grants. After the assisted housing programs discussed above, the next largest component of the HUD budget is the Community Development Block Grant (CDBG) program. These grants, which are received and spent on the basis of local priorities, include the acquisition and disposition of real property, construction of public facilities, rehabilitation of housing and the provision of a number of permitted public services. To be eligible, at least 70 percent of the funds received by a grantee must benefit individuals of low- and moderate-incomes.

As in the case of the programs discussed above, CDBG grants are largely project-oriented and subject to all of the criticism thereto. Moreover, implicit in their use is the presumption that communities can spend their way to prosperity and that the only impediment to economic development is the absence of a few more infrastructure projects that would attract jobs, technology and investment capital. We have long since stopped believing this about foreign aid and should now extend the same

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[7] CBO study, p. xix.

[8] "The Departments of Veterans Affairs and Housing and Urban Development, and Independent Agencies Appropriation Bill, 1995," U.S. Senate, 103d Congress, 2d Session.

skepticism to our domestic bricks and mortar development initiatives such as the Community Development Block Grants, the Economic Development Administration, the Appalachian Regional Commission and the Pennsylvania Avenue Development Corporation, to name several of the largest.

In the last few years a new class of local leaders has emerged who recognize that the cities have often been their own worst enemies and that the high cost of low-quality municipal services has been one of the main reasons why businesses and middle-class families have fled the cities and continue to do so in response to gross mismanagement. But new mayors in Philadelphia, Milwaukee, Los Angeles, Indianapolis, Cleveland, New York, and Charlotte, and Governors in New Jersey, Massachusetts and Wisconsin, to name just a few, have come to recognize that the key to their own development is not millions of dollars of federally funded projects but tax relief for their productive citizens, secure property rights through less crime, more efficient government that delivers quality services at the lowest price, welfare reform that ends long-term dependency, and a functioning school system.

These initiatives can only be implemented by local leaders, not by Washington. Indeed, to the extent that Washington's money can temporarily patch over problems or pretend to address needs, there is less incentive for local leaders to make the tough decisions needed to solve their problems. For these reasons, the CDBG program should be terminated in favor of local-based reforms that create an environment that encourages business and productive citizens to remain in, or return to the cities.

Federal Housing Administration. The Federal Housing Administration (FHA) was created in the 1930's to promote the then innovative long-term, fixed-rate, level-payment, fully amortized mortgage, and to fill the mortgage insurance gap created by the depression-induced collapse of the private mortgage insurance industry. Today, FHA competes with many private, taxpaying mortgage insurers for the profitable business of insuring mortgages on single family residences. While for most of its history the single family portion of FHA has been financially healthy, significant losses were incurred in the 1980's as the real estate market turned down in some regions of the country. Since then, as a result of an improved real estate market and program reforms, financial solvency has returned to the program and its net worth is estimated at over $4 billion.[9]

In addition to its single-family business, FHA also insures multifamily residential mortgages used to finance low- to moderate-income subsidized housing projects that were constructed under various HUD programs in cooperation with non-profit and for profit developers. In recent years, many of the poorly conceived and mismanaged multifamily housing projects have gone into foreclosure, leaving FHA and HUD with multibillion dollar losses.

This report proposes that the financially sound portion (single family) of FHA be privatized, and that the remaining risky, unsound insured multifamily mortgages be pulled from FHA and placed in a separate liquidating facility and the insurance obligation on these multifamily loans be transferred directly to the Federal Government. Otherwise, the ongoing risk of these multifamily mortgages might eliminate any private sector interest in acquiring FHA or diminish its price. It should be noted that there is precedent within HUD for such asset and obligation transfers to enhance the attractiveness of enterprises slated for privatization. In the late 1960's when the Federal National Mortgage Association (FNMA, and then a part of HUD) was scheduled for privatization, its risky, subsidized multifamily mortgages were transferred to a newly created entity within HUD, called the Government National Mortgage Association (GNMA), for an orderly liquidation.

Opponents of the above proposal would argue that the FHA is largely responsible for insuring the mortgages of creditworthy but moderate-income households who might otherwise not be of interest to private mortgage insurers. They further argue that promoting home ownership is still a national goal, and to the extent that FHA can help accomplish this at no cost to the taxpayer and without offering unfair competition to private insurers, then FHA should remain within the government in the belief that if privatized, it would turn away the otherwise creditworthy households of modest means. To the extent that this claim has validity, then a reconstituted FHA could be chartered as an independent government corporation (similar to FNMA) with no claim on the U.S. Treasury, required to be self-funded, and limited

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[9] "Mortgage Financing: Financial Health of FHA's Home Mortgage Insurance Program Has Improved," Report to the Chairman, Subcommittee on Housing and Community Development, Committee on Banking Finance, and Urban Affairs, House of Representatives, United States General Accounting Office, October 1994. p. 4.

to those households and houses that might otherwise be neglected by the private sector.[10]

Whether private or an independent government corporation, it is essential that a reformed FHA be free of day-to-day government meddling. Otherwise, FHA will continue to be exposed to the claims of special interests who, acting through previous Congresses and administrations, induced FHA to insure risky high loan-to-value mortgages, vacation homes, private investment properties and risky, subsidized multifamily projects.

Office of Fair Housing. HUD's Fair Housing program is tasked with the goal of enforcing the nation's fair housing laws and objectives, particularly as they relate to the ongoing problem of racial discrimination. Notwithstanding the considerable progress that has been made in this effort since the enactment of civil rights legislation in the 1960's, the problem persists and government has an obligation to enforce the law and encourage landlords, builders, and real estate agents to obey it.

Unfortunately, in attempting to meet this goal, HUD bureaucrats have trivialized the objective, and in their pursuit of subliminal violations, have opened the goal of nondiscrimination to ridicule.

How silly is HUD's effort? In response to HUD's directives, the Virginia Association of Realtors, for example, urged its member agents to use "caution" in the use of such words and phrases as desirable neighborhood, handyman's dream, near country club (although "near golf course" is deemed acceptable), prestigious, quality neighborhood, secure, and within walking distance. Listed as "unacceptable" are such expressions as able-bodied, bachelor pad, empry nesters, mature couple, mature individuals, near church and quiet tenants.[11]

In light of this and other instances of wasted resources by HUD, Congress should transfer the responsibility for enforcing the nation's fair housing laws to the civil rights division of the Justice Department where the issue can be more professionally handled in the context of comprehensive civil rights enforcement.

RURAL HOUSING PROGRAMS

Although the bulk of America's urban and suburban housing assistance is provided through programs administered by HUD, special purpose housing programs are administered by other Departments including Defense, Veterans Affairs and Interior, while rural-based housing programs are provided by the Department of Agriculture through the programs of the Farmers Home Administration.

As a consequence of their depression era origins, rural housing programs are markedly different than the suburban/urban programs of HUD, in part reflecting the depression's destruction of large segments of rural America's financial system. Whereas the FHA insured the privately-provided mortgages for urban and suburban home buyers, the Farmers Home Administration (FmHA) actually provided the loan, and usually with a significant interest rate subsidy. In addition, whereas a variety of multifamily rental assistance programs are the predominant form of housing assistance provided by HUD to low- and moderate-income urban and suburban households, the FmHA largely provided home ownership assistance, even to rural low-income households by way of deeply subsidized interest rates, in the belief that rental units were not always available in rural settings.

While the emphasis on single family housing has largely freed FmHA from the major financial fiascoes periodically associated with HUD's multifamily programs, FmHA, in contrast, bleeds from a thousand minor wounds. As GAO studies point out, many FmHA programs consistently suffer from high loss and delinquency rates, and have been poorly managed. Loan servicing by FmHA is costly, ineffective, and deficient in timely and accurate information. Recent experience with private servicing of FmHA loans indicates that improved servicing of $18 billion in loans yielded 5 years savings of $1.2 billion in servicing costs alone. Moreover, better private sector management led to a halving of the delinquency rate and an 80 percent decline in foreclosures.

With the passing of the depression and the re-emergence of private financial institutions in rural America, the low-income assistance responsibilities now attempted by the FmHA should be folded into the new housing block grant program proposed earlier, while the home ownership programs, whether by direct loans or guaranteed

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[10] See "Privatization: Toward More Effective Government," pp. 30–32 for a more detailed discussion and proposal for an FHA better targeted toward buyers of moderate incomes.

[11] Perhaps recognizing that the debate within Congress to terminate HUD was serious and that the public ridicule induced by the antics of the Fair Housing staff offered one more reason why the Department should go, HUD, in January 1995, issued a "clarification" which, among other changes, will again permit housing ads to use such terms as master bedroom, great view, Santa Claus, St. Valentine's Day and family room, among others.

loans, should be terminated and replaced by the same FHA programs provided to urban and suburban buyers.

TRANSITION ISSUES

As noted earlier, any major shift in HUD responsibilities and programs must be coupled with an orderly withdrawal from the many long-term commitments and contracts HUD has made directly with housing assistance providers—such as developers, nonprofits, local housing authorities—and with the assisted households. Most of the project-based programs involve some form of a long-term contractual commitment by HUD to subsidize some facet of the project such as the interest rate on the mortgage or the rents paid by tenants. In other cases where the commitment is informal, as is the case with public housing, many public housing projects have become dependent on HUD operating subsidies and modernization grants, and their swift withdrawal would have its harshest effect on those least able to bear it—the low-income residents of these projects.

In his Reinvention Blueprint, Secretary Cisneros proposes to deal with this problem by providing vouchers to the tenants of these public housing projects, allowing them to move to better accommodations and forcing the public housing authority to compete with private landlords for the rent money of the assisted households. This is an excellent idea, but with HUD dissolved, this should now become the responsibility of the states and funded out of the block grant they would be receiving.

With the states now in charge, another interesting opportunity for fundamental reform would be to give these same tenants more choice beyond staying or moving, by giving them the opportunity to use their vouchers to take over the management and ownership of the projects in a process developed during the Bush administration by HUD Secretary Jack Kemp.

The tenants in other types of subsidized projects whose contracts are expiring—such as those in section 8 new construction and renovation—would receive vouchers that they could use to remain in the project, or look elsewhere. Likewise for other types of projects and for those threatening to default on their FHA-insured loan.

CONCLUDING THOUGHTS

As noted earlier, many of Secretary Cisneros' proposals are commendable, and if enacted would constitute one of the most significant reforms ever imposed on HUD. As a result, it is tempting for some HUD critics to declare victory and give HUD a second chance. Congress should resist the temptation for two important reasons:

First, from just a budget efficiency standpoint, Congress should recognize that any reforms enacted today can easily be undone tomorrow by another Congress indebted to other interests. By continuing to maintain a "reformed" HUD with most of its project-based programs still intact, albeit at much more modest levels of activity, the seeds of a future expansion remain and would be difficult to stop in a different political environment. But with HUD dissolved and with basic decisionmaking and operations now transferred to the state level, it would be much more difficult, if not impossible, to expand and revive these costly and wasteful programs; and

Second, and more important, consolidating HUD resources into a block grant is an integral part of a comprehensive welfare reform program designed to move people into productive self-sufficiency, not to more efficiently inventory the poor by way of large scale custodial programs. With most of its programs purportedly targeted to low- and moderate-income households, HUD is an integral part of toady's welfare system and, thus, must be an integral part of any reform effort.

Mr. HERGER [presiding]. Thank you very much.

Without objection, both witnesses' full written statements will be included in the record.

Mr. Utt, you have put forward some well-constructed reform proposals today. The Clinton budget claims $51 billion in savings from 1996 to the year 2000, but overall, the HUD rises from $25.8 billion in 1995 to $36.1 billion in 1998, then falls back to $30.3 billion in the year 2000. That is hardly what most of us would consider cost savings.

With this in mind, could you trace some of the cost savings, specifically, of some of the reforms in your proposal?

Mr. UTT. If you break out the HUD budget, what you see is that most of the money is going to prop up the very costly project-based

type of housing assistance, whether it is public housing or old section 236 or old section 8 type housing, as well as those things operated under the HOME program.

As past studies of HUD activities have indicated, project-based financing is about twice as expensive as household-based assistance, per household served. So, by simply shifting from one form of the assistance to another, you manage to save a lot of money or manage to assist many more households with the same amount of money.

Just going through some of the budget numbers this morning, you can see what sort of additional and ancillary costs the commitment to project-based housing has incurred. As I think we are all familiar, crime has become a very serious problem in a number of the large public housing projects in some of our urban centers. The consequence of this is that HUD now performs a police-type function. In the last budget, $315 million was allocated toward drug prevention and crime control in the HUD budget.

If HUD could somehow figure out how to get out of the crime control business, those moneys could have been used to assist approximatelv 70,000 additional households. As I think we also know, HUD is not an entitlement. It is a rationed, means-tested program.

Again, these are the types of additional costs that are continued and perpetuated by continuing to link housing policy and housing programs and budget expenditures to programs that simply have not worked.

Mr. WEICHER. If I could add something to that, Mr. Chairman, the reason the HUD budget is going up from now until the year 2000, or up and down, as you pointed out, is because of the renewal of contracts on project-based assistance, contracts which will expire over those years and which will be renewed, and also contracts for voucher and certificates.

Budget authority in HUD is erratic from year to year, simply because contracts don't expire, don't terminate and get turned over on a regular basis. I think the reform that is proposed for low-income housing will gradually make that problem less. I think you can address that over the next few years.

Mr. HERGER. Thank you very much.

The gentleman from Minnesota, Mr. Sabo.

Mr. SABO. Thank you, Mr. Chairman.

Mr. Weicher, I appreciate that comment, because one of the real problems, whenever we have talked about HUD budgets, people mix up outlays and budget authority [BA]. Whatever serves their purpose from wherever they come in the ideological spectrum, they will, at times, talk BA and other times talk outlays. There is no program where the variation in BA is greater than HUD, and the comparisons are not easily made.

If you are talking about a 15-year certificate, you have 15 years of BA; for a 5-year certificate, you have 5 years of BA; and for a 2-year certificate, you have 2 years of budget authority. The outlays over a 15-year period are probably the same. It is the same with construction. You are talking full construction costs in the first year versus renting for 2, 5, or 15 years. So the comparisons are not easily made.

Let me ask about the whole question of construction. I haven't served on the housing committees here, but I have significant interest in housing from my State legislative days. I concluded early on that wherever the Federal Government was, it didn't begin to meet the needs of housing in this country, particularly for lower-income and moderate-income people.

I think there is virtue to the voucher plan, but from what I know of the needs in my community and my State, there is also really a need for new construction, not the big project types that we did at one point. My observation is that many, particularly the senior buildings that were built for seniors that were fairly intensive high rises, worked very well until we started mixing seniors with non-seniors. That was an absolute disaster, and we have reversed that.

But as I look at what exists in our city, there is really a need for the SRO's, the single room occupancy housing. This existed 30 or 35 years ago, but disappeared in the renewal or whatever happened in the cities. There is a real market for it but it is probably not going to happen without public assistance.

Within our metropolitan area, unless there is some assistance for building low- and moderate-income housing, all the trends of the market forces drive all of the people having vouchers into certain areas, the center city and inner-ring suburbs. The major problem we face is the suburbs with the greatest economic development are also the ones who have been developing housing policies that simply don't accommodate low- and moderate-income people. A person could have the voucher, but there is no place to rent, simply because of what has happened with the nature of their decisionmaking process.

Frankly, in our State, our rural communities are discovering, particularly the ones that have had the most aggressive economic development, getting jobs that pay $15,000 or $20,000 a year, that they don't have housing and companies are moving elsewhere simply because with new construction that is unsubsidized, people in that job range can't afford to buy. The old housing is at a market level that is lower than that, but that is bought up.

So we have a Republican Governor in our State who is suggesting housing subsidies to buy down the cost of developing housing units in smaller rural communities.

Mr. Weicher, in particular, I would like you to respond to that, because I think we can get caught up in theory and not deal with what really exists.

Mr. WEICHER. I would be glad to, Mr. Sabo. Let me start with your comments on the voucher and certificate program first, and then go to the cost comparisons.

There are more of the people with vouchers and certificates who live in the suburbs than there are people in public housing who live in the suburbs. Forty percent of the people who have vouchers and certificates use them to live in suburban housing. On average——

Mr. SABO. If I could interrupt there, that is probably true, but it is only certain types of suburbs.

Mr. WEICHER. I don't think that is true, with respect——

Mr. SABO. It really is in our area.

Mr. WEICHER. The information that we have from surveys of voucher and certificate recipients shows that they really do work

in all kinds of markets. Among other things, we did a survey of Montgomery County a few years ago which showed significant use of vouchers and certificates, a high rate of success among lower-income families using their vouchers and certificates to rent housing in Montgomery County, which is not cheap, but it is also not an inner-range suburb, in any sense. Very little of it is.

There are, in fact, more vacant rental housing units in the United States renting for less than the fair market rent than there are occupied public housing units or occupied voucher and certificate units, for that matter. So if you were to terminate public housing tomorrow and everybody now in it chose to move—and certainly, everybody now in it will not choose to move, particularly not the elderly households and not the disabled households—those families could, in fact, move to housing that they could afford with a voucher or a certificate.

We have almost as many voucher and certificate units now as we have public housing units. It is 1.1 million versus 1.4 million. We have had that program for 20 years. We have had it almost as long as we have had most of the social welfare programs in this country, and it works quite well and the success rate continues to rise. Every voucher that you authorize is used by someone to rent decent housing somewhere in the private market.

Mr. SABO. I don't doubt that that housing is available. Again, I have to go on my experience. I come from a large county. It has a center city. It has the inner-ring suburbs, and then the developing ones. There is no doubt that if you gave everyone vouchers, there is housing available, but it would all be in the center city. And, it would be in those inner-ring suburbs. It would not be in the suburbs that had the most housing growth. It would not be in the suburbs that had the most job growth.

So you could even look at the county numbers and you could exclude the city and you would probably find it available, but you would still have just an incredible polarization of where that housing exists. It is a very fundamental problem.

You look at the correlation of what has happened with housing development and crime, and, frankly, if we wanted to deal with crime issues, housing is what you would deal with. When you concentrate poor people in certain neighborhoods, the crime rate escalates.

That is why I have the problem with this theory and why, also, I have some concern that I am not sure where the administration is headed on the question of construction. Where it is needed, there is desperate need for assistance in moving that housing around the suburban areas, or it leads to incredible social problems.

Mr. WEICHER. The current cost of building a new public housing unit in the HUD budget is $85,000. The interest on that, since you are going to have to finance it by borrowing, is about $6,000 to $7,000 a year at today's Treasury borrowing rates. In addition to that, you would have operating subsidies of a couple thousand dollars, and, ultimately, you would have modernization expenses, and they wouldn't come very far down the road. At least, they wouldn't, based on past experience.

That is over $9,000 to begin with and it is going to grow. Operating subsidies have more than doubled in the last 15 years, and 15

years ago, they were supposedly being inflated by the fact that we had an oil embargo and the cost of energy was so high. You have a large and growing expense for every public housing unit you build—50 percent above the cost of a voucher or a certificate.

Not many subsidized units, under any program, are really built in outlying suburbs. They have not been built under any of the production programs that we have had in the past. They haven't been built in public housing.

Mr. SABO. No, I know that.

Mr. WEICHER. If you adopt the idea of a construction program and say, we are going to have the Federal Government going back to the section 8 new construction idea, going back to subsidizing production of housing for low-income families and put it in the outer suburbs, you will find that most of that housing, if it is built anywhere near the outer suburbs, will be elderly housing. It won't be housing for people who may be looking for jobs in the outer suburbs.

I think you are comparing, if I may say so, a kind of an idealized view of how project-based assistance works, and I am thinking about the actuality of a mess at HUD where $25 billion of insured assisted projects out of a total HUD insurance of half a trillion dollars, that $25 billion is a tremendous drain on the Treasury and a tremendous drain on what HUD does and doesn't provide particularly attractive housing over a long period of time. We have 35 years of experience with that kind of program.

Mr. SABO. I am not looking at the big projects. I think they are a thing of the past. I don't think anyone quarrels with that. But there is desperate need for new construction that is family-based, so that you have some capacity to develop some diversity of housing and deconcentrating the poor folks in certain types of cities and certain types of suburbs.

I am not sure how we are going to get there, and I don't know how that kind of program should be structured. Maybe it shouldn't be ongoing. Maybe it should be a write-down of the initial costs. I don't know, but it is a need, and if we simply move away in total from that need, I think we do significant harm to the nature of urban development in this country. We probably have a larger impact on urban development and how it occurs, than on the availability of housing for a particular person, because that is going to be available but it is all going to be concentrated in some geographic area.

Mr. Chairman, I have taken more than my time.

Mr. HERGER. Thank you very much.

Next to inquire will be the gentleman from Colorado, Mr. Allard.

Mr. ALLARD. Thank you, Mr. Chairman.

I would like to address this question to both Mr. Utt and Mr. Weicher. As you know, we are looking at abolishing four agencies, HUD, Education, Energy, and Commerce. Could you share with this committee how we could most efficiently eliminate HUD? For example, what are we going to do with FHA?

Mr. UTT. I have sketched out a blueprint for such a proposal in the testimony that I submitted to the committee and added some details for that. My proposal is to take all of the targeted, means-tested, low-income housing assistance that is now operated through

a variety of different vehicles by HUD and accounts for approximately 80 percent of HUD's budget and put that into a super welfare block grant that would be distributed to the States to be used for purposes of housing, income assistance, at the discretion of Governors, wherever the need was the greatest.

One advantage of that, which, I think, addresses some of the concerns that Mr. Sabo said, is that with a block grant, you are no longer imposing a one-size-fits-all policy on communities. You have some communities that are growing faster than others. There is a housing shortage there. The poor or those with more modest means, even with vouchers, may find it difficult to find suitable housing. So in those places, the Governor could use his discretion and, as appropriate, fund or subsidize some form of new construction.

In other parts of the country where population is declining for one reason or the other, one would expect growing vacancies, and with growing vacancies, falling rents, and so housing is a less critical issue in those areas but jobs are. So more money could be spent for income assistance and food assistance rather than housing assistance.

But it gives a lot of flexibility, because there is a national market, but there are wide divisions and extensive diversities within individual communities regarding their particular needs. So I would put all this in a block grant and urge it to be used, to the greatest extent possible, for household-type assistance.

That kind of block grant also makes redundant what is HUD's second-largest program, and that is the community development block grant program, which, again, is largely a housing assistance program operated at the discretion of mayors and Governors and, again, targeted toward low-income communities.

That leaves FHA as the last and largest segment of HUD. I would make that an independent government corporation with a very restricted mission, and that is to facilitate the home ownership opportunities of individuals who might not be served—who are creditworthy and reliable but who might not now be served by the private mortgage insurance or the private lenders because of perceived risk. This is the historic role that FHA has had and one that they have demonstrated they can become financially self-sufficient, if they fulfill it.

Mr. ALLARD. I don't think that the concept of having the tenants go ahead and buy a home or apartment that is now public housing is that far out. For example, Margaret Thatcher in England, did some of that.

I guess my next question is, how do we go about this process of converting public housing into private home ownership? Could you go into a little more detail on how we might do that?

Mr. UTT. In terms of the public housing?

Mr. ALLARD. Yes.

Mr. UTT. I think the proposal in the budget to provide the residents of public housing units with a voucher that they can either use to remain and pay the rent in the public housing project or to seek housing elsewhere, in another part of the community, is a logical step in the direction of giving them the option of collectively

acquiring that public housing project and managing it on their own.

You have several such experiments that have been underway, one in Washington, DC, and another in St. Louis that, I believe, are relatively successful in terms of tenant management and ownership. By granting everyone a voucher, they now have the financial wherewithal to engage in the self-management of that organization and choose how to spend their own money.

I would certainly not impose it on anyone. I think it works in some situations and doesn't work in others, but I would clearly leave it as an option for the tenants that they might choose to avail themselves of.

Mr. WEICHER. If I could respond on that?

Mr. ALLARD. Yes, sir?

Mr. WEICHER. We dealt with this idea very substantially in the last administration. This was one of Secretary Kemp's ideas and something we worked on very much at HUD and were able to bring to fruition in a number of areas, and we had a program in place to expand it, which, unfortunately, has been basically terminated in this administration.

I think that there are really two things that can be done in terms of allowing tenants to buy their own homes in public housing. The first is that 100,000 public housing units are single-family homes. That is easy. We know how to create home ownership in single-family homes. Providing them with a voucher provides them with the ability to make the mortgage payment on that home quite easily.

Secondly, in conventional public housing, what we think of, the kind of project that Mr. Sabo, for instance, had in mind as something we didn't want to do any more of but which we certainly have a lot of in existence now: most of those units have already been paid for by the Federal Government or the Federal Government is going to finish paying for them. I believe there is about $700 million a year in bond payments that the Federal Government is making on them, but that is not a large amount of money anymore.

So what you are dealing with is the tenants need the ability to pay for the upkeep and to pay for whatever modernization is needed. In some of the projects where a lot of modernization is needed, it is not going to make a lot of sense to spend that money, whether you are a tenant or whether you are an owner in a co-op or a condo, and I think those projects can and should drop out of the inventory. But those are the projects that people tend to have in mind.

There are other projects where not as much money needs to be spent on modernization. They are in reasonably good shape. That is particularly true in smaller cities and rural areas. There, if the tenants want to create a cooperative, create a condominium, create a management association, which many of them already have as the first step, then it is not that hard to use these resources to create home ownership opportunities.

Mr. ALLARD. Thank you, Mr. Chairman.

Chairman KASICH [presiding]. Thank you.

Mr. Coyne, please.

Mr. COYNE. Thank you, Mr. Chairman.

Mr. Utt, with regard to your response to Mr. Allard about consolidating programs at HUD and providing assistance to local communities in the form of block grants, do you think it would be necessary to put a lot of requirements in the legislation that that money be spent for housing, or would you feel that the local officials would just do that as a matter of course?

Mr. UTT. That is a very interesting question. While I would like to give Governors as much flexibility as possible, because I think the housing situation in every community is dramatically different from one to the other and it is very difficult to make judgments in Washington as to whether 15 percent or 40 percent should be in housing, rather than have requirements, I would like to see some sort of standards or desired outcomes established that would measure success, with the opportunity to redirect that money or push it in another direction.

I just don't think that, in Washington, you can make decisions as to how much income assistance Cincinnati needs versus how much housing assistance it needs, and I am just afraid that any requirements would probably cause more problems than they help.

Now, as part of our comprehensive social safety net that the Federal Government and State governments provide, HUD programs are a very small portion of that. We calculate that means-tested programs in 1993 provided by the Federal and State governments amounted to about $324 billion, of which HUD and housing accounted for about $30 billion of that. So it is only about one-tenth of it.

I would say that if you needed a requirement, simply matching that 10 percent provision might be enough flexibility, but with an opportunity for a Governor or a mayor to have some opportunity to grant an exception in a timely fashion, provided that certain information and formal requests are made in this regard.

Mr. COYNE. I guess, in the absence of putting specific language in legislation about what it is supposed to be used for, I could envision some people who need a street repair program using it for asphalt.

Mr. UTT. Precisely. That is what I said. This would be a welfare-oriented program, toward human assistance, and it couldn't be used, hopefully, to build libraries or weekend cottages or trim hedges in parks, but it would be oriented toward basic income assistance, food assistance, et cetera.

Mr. COYNE. Thank you.

Chairman KASICH. Let me ask a question of Mr. Weicher, and then we will go to Mr. Miller.

I understand, Doctor, your concern about what we need to do to the private section 8 operation. If, in fact, we say to these folks, we are going to give you market rates, which I am becoming convinced is the way to go, and they begin defaulting and we are holding the mortgages, and maybe we have to do this, if they start defaulting and we start getting these mortgages, we could potentially lose a ton of money, couldn't we?

What you are saying is, either way we go, we are going to lose a ton of money. Let us not throw good money after bad. What is your sense as to how we get out of this situation, or should we take our hits? What do you believe the potential cost of this is?

Mr. WEICHER. That is the multibillion-dollar question. The best estimate I know of the—let us start with the total value of multifamily insurance that is in force on assisted housing units. The IG reports that it is about $25 or $24 billion, three-quarters of the HUD-insured inventory that is actually multifamily. There is $44 billion at HUD that is multifamily insurance, speaking broadly; $32 billion of that is really multifamily; the rest is nursing homes and hospitals and all sorts of odds and ends. About three-quarters of that $32 billion is for insured assisted projects. That is $24 billion. That is the most you can lose.

I don't want to say that is chicken feed, but that is $24 billion that could default over about the next 15 years.

Chairman KASICH. What is your sense of how much of that would actually default? In other words, say you have these people out there that are scamming the system. They tell you, if you reduce my payments, I am going out of this. Would they?

Mr. WEICHER. I think it would be interesting to find that out. We did a study in PD&R at HUD when I was there which came out in 1992 and which people still seem to be quoting, although they may have updated information, which suggested that about a quarter to a third of the insured projects had some problem with paying their capital maintenance needs, their capital maintenance and renovation needs, out of their income stream. The other two-thirds to three-quarters were not having that problem.

Now, some of those projects with problems could resolve the problems, and they may have resolved the problems. Others may have developed problems. And if you cut back the income stream, some other projects might develop problems as well.

But I think that suggests that, perhaps, half of the inventory, and here, that is a guess and I would ask the IG and GAO and HUD to give you estimates on this, and I would press them for it.

Let me put that $24 billion, which is the most you can lose, in perspective. CBO has said that the preservation costs for the next 5 years will be $22 billion, and at the end of that time, you still have $24 billion in insurance outstanding. So the most you can lose, if the IG is right about this, and I think she is, the most you can lose is $24 billion.

I don't want to sit here and say to you that you should regard that with equanimity, but this isn't the Defense Department that we are dealing with here and it isn't Social Security. You are going to be asked to appropriate very nearly that amount of money just to keep these projects going over the next 5 years.

Chairman KASICH. And the mark-to-market program is designed to begin to get at this, but you believe that that is, in fact, throwing good money after bad. Could you run through that very quickly, logically through those steps, as to why you would not do that?

Mr. WEICHER. I think, in the first place, I doubt very much if HUD has the information to make judgments as to how much it will actually cost to mark these projects to market. As I said, they don't do a particularly good job of underwriting multifamily projects in the first place, and they aren't going to do a very good job of re-underwriting multifamily projects when they have to sit down and do it.

You can make sort of broad estimates on a sample basis, which may work for budgeting purposes, at least, with some degree of error, but they are going to have to sit down and go project by project through 14,000 projects, and somebody is going to have to go through all the financial information on those projects. I know from my experience, and I read in IG reports, that HUD does not have very good financial information on these projects.

Indeed, the No. 1 material weakness that the IG identified when we were there was the lack of information on a management accounting system for the section 8 projects. We set in place a system to remedy that defect, which has carried on into this administration and they are continuing it, but the IG said last September, I think the quote is, "Progress is slow."

I don't think they have the information to make the judgment. I think a team would have to sit down and go into each project and try to figure it out, and then they would have to negotiate with the landlord and with the lender. Anything you give the landlord which is more than it is going to take to keep that project in use, you are wasting money, but it is going to be very hard to judge that. Anything you give the landlords that is less than the amount that it is going to take to prevent a default, you are throwing it away and you are going to have to——

Chairman KASICH. So what you would suggest is, what we do with this multifamily assisted program is, essentially, reduce the payments to the market rates and let the chips fall where they may?

Mr. WEICHER. That is right, and the chips will fall over a period of about 15 years, according to the best information I know about when these projects are likely to have their current contracts expire.

Chairman KASICH. Finally, since the Secretary is talking about moving toward a full voucher program, it would be a total contradiction in terms to argue that we ought to have new public housing construction, correct? How could they put both of those in a budget?

Mr. WEICHER. What you have here is all the current public housing programs in the budget are consolidated into two block grants and one of them is a block grant for what is called capital purposes and they put modernization in it, but they also put the $598 million from the 1995 budget for new construction into that new capital fund.

That doesn't require public housing authorities to use that money for new construction, but that is $598 million that, based on the administration's program, you don't need to appropriate for that purpose and you can leave the modernization money at its present level.

Chairman KASICH. Thank you.

Mr. Miller.

Mr. MILLER. Thank you. I appreciate your testimony today.

To tie in with the whole issue of HUD and the welfare system, last fall, I was on the ballot in November, so I was able to spend some time studying welfare issues down in my district in Florida, I remember one morning I spent over at the office that does food stamps and AFDC. It was interesting. The workers' complaints

about public housing was once people got into public housing, they were locked into the welfare system. They had no control of it.

The problem when you are looking at the welfare issue, it covers so many different areas. Last night in appropriations, we zeroed out the LIHEAP program. There is program after program. The Agriculture Department has food stamps.

I know the Ways and Means Committee has already passed out a bill on welfare reform. Is Congress, looking at it from your think tank perspective outside, really looking at welfare in the comprehensive approach that we should be here? I am not an expert on it. I am not on those specific committees. Do you have any suggestions of this welfare overview? I agree with the block grant concept idea, but it really needs to be tied in with, I think, the food stamps and LIHEAP and AFDC and everything.

What is your perspective of not just looking at HUD in the narrow perspective but the big welfare picture, both of you?

Mr. UTT. I think there are already several pieces of legislation that have been introduced in this Congress, I think in the House by Representative Talent and in the Senate by Senator Faircloth, that would deal with the issue in a comprehensive way.

We have a welfare system that——

Mr. MILLER. But are we doing that?

Mr. UTT. The welfare system today has evolved into, from my perspective, a fairly costly custodial function, in which once you get into it, you are basically marginalized, put on the shelf, and taken care of, in some minimal way, for as long as you wish, for your life in some cases.

I think a welfare system ought to be designed to move people toward self-sufficiency, productivity, and a life independent of Federal assistance, and I think most people on welfare want that. But we have a system where the incentives are all in the other direction.

I would like to see, as the principles, whatever they may be, of any welfare reform as a program whose objective is not to cost effectively inventory people but to move people off welfare and into productive lives. It is my understanding, and again, I am not totally familiar with those two bills that I mentioned, that they have as their objective or as their goal, that particular objective.

Mr. MILLER. But I am getting concerned that we are approaching it too piecemeal.

Dr. Weicher.

Mr. WEICHER. A couple of things I might say. We at Hudson are involved—I am involved with some of my colleagues in an effort to help the State of Wisconsin design a new welfare system because they passed legislation terminating the AFDC program effective 1999, and we are working with them on a proposal which Governor Thompson hopes to finalize by mid-summer, I believe, and have introduced in the legislature.

My own sense of it, and this is not necessarily a final position that we will propose at Hudson, or, certainly, what Governor Thompson would say, but my own sense of it is what you need to do is you need to make sure that anyone who is on welfare is either learning or working at the same time that they are on welfare. You need to take the view that this is a temporary program and that

you should be acquiring the skills, whatever you need, and it may be experience and it may be education, so that you can become a productive member of society.

At HUD in the last administration, we had a program which we called Operation Self-Sufficiency, where we required a substantial number of the people who received a voucher or a certificate to enroll in education, if that is what they needed, or job training, if that is what they needed, as a condition of receiving the housing assistance and to meet specified targets, specified progress toward economic self-sufficiency, including getting a job and holding a job to remain eligible for the housing assistance. The program didn't work perfectly, but it worked reasonably well.

Mr. MILLER. I have one quick followup. But you were operating independent of the people running AFDC or the food stamp program or the LIHEAP program or what have you, right?

Mr. WEICHER. That is right.

Mr. MILLER. And part of the problem is that it is spread all over. You can't just solve it within HUD.

Mr. WEICHER. No. We tried, though.

Mr. MILLER. Thank you.

Mr. HERGER [presiding]. Thank you very much.

The gentleman from Utah, Mr. Orton.

Mr. ORTON. Thank you, Mr. Chairman.

I would encourage my friend, Mr. Miller, to take a look at the Self-Sufficiency Act, which I have filed. I think you would be very interested in it.

To our panelists, thank you very much for your opinions. Mr. Weicher, I would like to congratulate you on at least a portion of your conclusion about FHA, that its mission has not been fully accomplished, that it probably would not be picked up totally in the private sector, and that you oppose privatization. I concur with you.

I also agree that there are some problems in it and that we need to revise FHA in order to make it more functional. In that light, I will unashamedly encourage my colleagues to look at the bill that I have filed to reform FHA as well.

But I do have some concern over one part of your testimony, Mr. Weicher. On page 6, you attack the affordable housing fund, the HOME block grant program. You say, "It is not clear why there is a need for a new program of building low-income projects when we appear to have bipartisan consensus that the concept itself is flawed and certainly is inferior to the voucher program."

I do share your concern over project-based public low-income housing in general. However, let me share with you an experience on the HOME program specifically.

I am a member of the Banking Committee. The Economic Growth Subcommittee held a hearing last Congress in my district in Salt Lake City. The city of Salt Lake is not unique, in that it has a very high occupancy rate and a very low vacancy rate. The cost of housing is quite high. In fact, approximately 50 percent of the people living in the homeless shelters have jobs, but they still can't afford to find affordable housing.

In this light, we took a tour of a particular project called the Smith Apartments. This was an old apartment building, previously

run down, vacant. Through a joint venture between the Salt Lake Housing Authority, the affordable housing program fund, a private sector contractor, and a bank, using seed money from the HOME program and leveraging that with private capital as well, they renovated this project. It is now rentable and the people living in it are families who previously were homeless. The program is working very, very well. This is an excellent project in Salt Lake City.

My concern is that it appears to me that the HOME program is exactly the kind of approach that you and my other colleagues would normally be praising, particularly since it is done through a block grant with more local control and decisionmaking authority.

So I am wondering if your attack on the HOME program is based on theory or if it is based on a study of specific projects that have been funded by the HOME program, knowing it has only been in existence for 3 or 4 years. I am wondering if you could share with us the specific projects that you have looked at that have been funded under HOME, and share with us the information that you have used to reach the conclusion that this is a bad program and just ought to be zeroed out.

Mr. WEICHER. I am not a theorist, Mr. Orton. I have spent 7 years at HUD, and at that point, you are not a theorist anymore.

First of all, you can do rehabilitation of low- and moderate-income housing under CDBG, as you can under HOME. There is nothing magic about HOME.

Mr. ORTON. But also, under CDBG, in my district, our mayors, along with the Governor, are using CDBG for parks, for water runoff projects, and for a variety of things. They don't have to use it for housing.

Mr. WEICHER. That is right, but the main use of CDBG continues to be for housing and for housing rehabilitation and renovation, and the main use for HOME is also housing rehabilitation and renovation.

My evidence for that is an evaluation which is being conducted at the Urban Institute under a contract which we let when I was at HUD. The project investigator, at a public seminar about 3 weeks ago, said that, basically, HOME is being used for the same purposes as CDBG is being used for. That is based on national information. That is not based on looking specifically at Salt Lake City and going project by project, but it is based on an evaluation of projects and activities all over the country.

I don't see that there is good reason, as I said in my testimony, I don't see that there is good reason to be spending double the amount of money on these purposes that we were spending 5 years ago, and I think the combination of HOME with FHA insurance is going to create headaches for all of us.

Mr. ORTON. I know that my time is expired, Mr. Chairman. If I could ask leave to ask the witness if he would submit to this committee the specific data that he has suggested, that is analyzing specific projects funded under HOME so that we might have the information available to see and judge as well.

Thank you, Mr. Chairman.

Mr. HERGER. Without objection. Thank you.

The gentlelady from North Carolina, Mrs. Myrick, will inquire.

Mrs. MYRICK. Thank you.

I have several questions. When we are talking about the multifamily default, I believe, Mr. Weicher, you said that HUD has roughly 14,000 projects in multifamily.

Mr. WEICHER. That is right.

Mrs. MYRICK. Is there any way you can just give a rough percentage estimate of this? How much housing stock do you feel could be rehabilitated for home ownership, affordably? I know HUD has a list right now of multifamily projects that are supposed to be imploded or destroyed, several thousand units, anyway. How much, including what is already slated for destruction, do you feel would just be totally useless?

Then I have a third question. Those 2 percentages, if you can give me those, and then the third part is, there are some areas of the country where there are HUD projects on very valuable land relative to economic development, and I know this gets into an issue that a lot of people don't want to talk about, but the point is, there are ways that that land could be sold and receive some good amounts of money for it and then there could be housing provided in the community in other places, in smaller units, like scattered site, that type of thing, which, as you know, most communities are doing.

Do you think that that is a reasonable thing to look at, or does that just throw up red flags that cause a lot of problems?

Mr. WEICHER. Let me start with the middle question, because, I think, that is perhaps the easiest, although any numbers are going to be imprecise.

Mrs. MYRICK. I understand that, but I am just asking for rough estimates.

Mr. WEICHER. From both the way tenants evaluate the housing they are living in and what we seem to know about it from efforts to estimate the cost of rehabilitation and so forth, and from what we seem to know about long-term vacancies in public housing, perhaps 10 percent of the housing stock really is not worth trying to preserve in any use at this point.

Mrs. MYRICK. Right.

Mr. WEICHER. It may be something less than that, but there are projects which are basically vacant or nearly vacant and which no one really seems to think can be renovated. It is not a large share of the stock, but it is a noticeable share of the stock.

At the other end, I think the real question as to how many projects can be converted to home ownership depends fundamentally on how many people want to be home owners.

Mrs. MYRICK. Right.

Mr. WEICHER. I would say that in elderly projects and perhaps in disabled projects, it is very unlikely that most of those residents would want to own their projects. Owning your own home takes time and resources, and I would doubt that they want to. That is about 35 to 40 percent of the inventory right there.

In the remainder, I would think that perhaps a quarter might be rather expensive to renovate to the point where they would be satisfactory for home ownership. But, again, the history of the home ownership efforts we have are that determined groups of tenants have made projects work where all the conventional wisdom, including the conventional wisdom at HUD, is that they can't be

made to work. I wouldn't try to rule out anything until the residents told me that they couldn't do it or didn't want to.

Mrs. MYRICK. I have one other question. You mentioned for, again, home ownership, you said that there would need to be a certain amount of upkeep for these tenants. My question is, where would that money come from, and is this an ongoing thing? Are you looking at it like some kind of a subsidy that would need to be there on a regular basis to make these projects workable?

Mr. WEICHER. We proposed in the program we had in the last administration that there would be an ongoing commitment equivalent to the current operating subsidy for the tenants for a period of 5 years to enable them—for a period of time during which we would expect that they would be able to develop their own sources of income to support the project, to support the operating cost themselves on a continuing basis. I think we had a 5-year renewal option on that and that was it. But I think that you probably need something like that for transition purposes.

Mrs. MYRICK. Just one quick thing. When we were, again, talking about home ownership, you said, it takes the right person, of course. I know that, but has it not been done more simply because the right people aren't there or because the idea hasn't been put forward to the extent that it could be?

Mr. WEICHER. I think it is the latter. We had expressions of interest in home ownership and in resident management of public housing projects from all over the country. I don't remember the numbers anymore, but we had many, many residents writing in and many resident management groups writing in and saying, "We want to do this. We would like some help. What are you doing? Come and talk to us."

Mrs. MYRICK. Thank you very much.

Mr. HERGER. I thank the gentlelady.

The gentleman from Kansas, Mr. Brownback, will inquire.

Mr. BROWNBACK. Thank you very much, Mr. Chairman.

Thank you very much for coming in front of the committee. We appreciate that.

The current Secretary of HUD says we need to reinvent HUD because of problems in management, problems in ownership, problems in fulfilling its mission. Both of you have been around a while. How many times has HUD been reinvented, that you know of, since 1965, legitimate efforts to say, it doesn't work, so let us make it different?

Mr. WEICHER. Ron and I came to HUD at the same time, in 1973. That is where we first met each other, and as he said, we came after a wave of scandals, when Secretary Romney commented, as he finished his 4-year term, that he thought HUD should be abolished. There was a substantial redirection of housing projects and that is when the voucher and certificate program was created.

There was not a major change in policy again until 1989, when we had another wave of scandals and we developed major reforms in the administration of HUD and also developed the home ownership efforts that we have just been talking about. But in between, there was a shift away from public housing and toward the vouch-

ers and certificates that went on over that period between the 1974 act and today.

I would regard Mr. Cisneros's proposal as the third serious attempt to reinvent HUD in the last 20 years. Under President Reagan—you could count that as well—there was a substantial consolidation or elimination of programs and they did terminate the section 8 new construction program in 1983. Three, maybe four, in 20 years.

Mr. BROWNBACK. One other thing that I wanted to ask about was that I looked in some GAO reports where HUD doesn't know the number of units it has. I can understand that cattle are hard to count because they move on you, but houses don't move—I guess you can move a house, but why don't we know how many houses we have, or am I behind the time and they now do know how many units they have and where they are?

Mr. WEICHER. I think this is the problem of management information systems that has contributed to the scandals that HUD has had over the years. The information on the number of units that are assisted under the various programs is typically available, if it is available at all, at the field office level, because the projects are assisted at the field office level.

HUD has not ever devoted adequate attention to the management side. We tried in the last administration and we made a start on it, I think a significant start on it, and the present administration is continuing that effort, but it is going to take a substantial, extended effort over several administrations to get that information basis firmly in place.

Mr. BROWNBACK. Thank you very much.

Thank you, Mr. Chairman.

Mr. HERGER. Thank you very much.

The gentleman from New Hampshire, Mr. Bass, will inquire.

Mr. BASS. Thank you, Mr. Chairman.

I have a brief question. I am not sure which one of you to address it to. I had an opportunity to review your testimony in which you are discussing the possibility of turning the housing programs into vouchers, block grants, trying to refocus housing on getting people better educated, entering the work force.

However, there is a group of individuals, as you allude to in your testimony, physically disabled or developmentally disabled sectors of the population, and the elderly. I think one of you made reference to that. They may not only not want to own their own housing, but they may be in no position to become either better educated or get a job.

In the context of your plans and your proposals, which, I think, are good and should be investigated, what portion of this whole problem is associated with these individuals? I would, perhaps, throw into that mix children, because some said they may be involved, although they will, hopefully, be part of the solution in that they will become better educated and they can enter the work force, but not until they get out of school.

How do we address that segment of the population from a housing standpoint in this plan to change HUD, perhaps permanently and for the better?

Mr. WEICHER. I think, on the elderly and most of the disabled, you really don't have a problem. The projects work reasonably well. The residents are reasonably satisfied. There is no particular reason to expect someone of 75 or 80 to go back into the labor force. That is not what we are concerned with.

At the same time, I think, if you give those residents the option to seek other housing if they want to seek other housing, I don't think that does them any harm and I don't think it does the projects any harm, and that is an area where I agree with the Reinvention Blueprint, as I indicated.

I think that with respect to children, the unit to think about is the household. It is the parent and the children, and the parent, in too many cases—not in all, by any means, but in too many cases—you have parents who are not particularly well educated and who do not particularly have much labor force experience and who aren't working and who need some way to get connected back to the labor force. I think that that gets us back to the welfare reform that, I think, was Mr. Miller's concern.

But I think that these households are in a position, again, to make judgments as to whether the housing assistance that they are getting is something that they would like to spend where they are now living, or something which they would like to spend somewhere else; and the people who have vouchers and certificates are very much like the people who live in public housing, about the same income level, about the same demographic composition, more of them in the suburbs than in the case of public housing. But these people have the ability to use the housing assistance to solve that part of their problem.

Mr. UTT. I just would add, in the context of welfare reform, that, yes, we make a distinction, certainly, between the elderly and the nonelderly able-bodied as well as those with young children and those whose children are somewhat older.

We have calculated, or, at least, my colleagues at the Heritage Foundation who are more knowledgeable about this than I am, have calculated that at least half of the households receiving AFDC support have no children under age 5 in that household, that is, that the children are all older and, therefore, presumably in school during the day, freeing the parent or parents for bona fide work or job training.

Mr. BASS. I have no further questions, Mr. Chairman.

Mr. HERGER. Thank you very much.

Mr. Sabo, would you like to inquire?

Mr. SABO. Thank you, Mr. Chairman.

Mr. Weicher, I am curious about the problem of HUD-acquired housing. I assume these are FHA-defaulted loans.

Mr. WEICHER. That is right.

Mr. SABO. They seem to have a terrible time disposing of them. Once they are in default and reacquired by the FHA, it takes forever to get them back and circulated into the market. They end up boarded up regularly, which really hurts neighborhoods.

Is there anything from your experience on how we can speed that whole process up? I guess you end up with the same thing with some of the VA-insured housing, also, that it sits vacant for a long time and is boarded up. FHA seems, at least in our area, to do

more of it. You go by it and you have HUD housing and boards on the windows.

Mr. WEICHER. I think you need to distinguish, here again, between single-family and multifamily, Mr. Sabo. Single-family typically, at least, in the last administration when I was tracking these numbers, the single-family defaulted inventory, the HUD-owned inventory, worked about like this.

You started a year with 40,000 houses in the inventory. You took in 80,000 houses. You sold 80,000 houses, and you ended the year with an inventory of about 40,000. On average, you turned over the inventory every 6 months.

But that doesn't mean that you sold every house 6 months after you got it. There are, unfortunately, a fair number of houses which stay in that inventory for a lot longer than 6 months and are boarded up and are eye sores and are blights on the neighborhood, and you have neighborhoods where you have a substantial number, and in quite a few cases—I come from the city of Chicago, and there are neighborhoods in Chicago where FHA launched a big program to promote low-income home ownership with special interest rates in the 1960's. There were huge defaults and foreclosures in those neighborhoods, and there are still boarded-up houses in those neighborhoods in sufficient area to constitute real neighborhood blight, three decades later.

But typically, FHA can turn over a single-family house within that period of time, and where you have a neighborhood, then you need some kind of effort to either tear those down and dispose of the land or to renovate those houses and sell them. We have had programs to promote home ownership in HUD-owned inventory and, sometimes, to give the houses to the homeless, and they make some progress, but again, you have to go neighborhood by neighborhood.

Mr. SABO. Are there specific problems in the rules on what they have to sell them for?

Mr. WEICHER. Not really. There are things you can do, and there are occasional set-asides for the homeless or for some other purpose. The law is that they should sell it for as much as they can get for it to minimize the loss to FHA, in order to protect the actuarial soundness of FHA. But, I think, what you have is that some houses shouldn't have been insured in the first place and it is hard to resell them. And in other cases, where you have had this kind of neighborhood program, you have a neighborhood problem.

Mr. SABO. I was just in a neighborhood on Monday, driving around, and there was this boarded-up housing. I was with the director of the neighborhood group. They have financing programs available.

Mr. WEICHER. You may have a problem in the local office, for some reason, that I wouldn't know about, but it has never been policy in this administration, the last administration, or any administration that I am familiar with, it has never been policy to hang onto these things. When you are HUD, one hears from you and your colleagues and from private citizens about these neighborhood problems.

Mr. SABO. My sense is, Fannie Mae and some of these other groups turn them over quicker than HUD does.

Mr. WEICHER. I am not sure that is true on single-family. We looked at this a few years ago and I didn't get the sense that there was any significant difference there, but they may have fewer—they are not buying loans as far down in the price distribution, as far down in the quality distribution, on average, certainly, as FHA is, and they may not have that bottom of the barrel, so to speak, that they have to deal with.

But I think that it was certainly true 3 or 4 years ago that they weren't doing particularly better than FHA. They weren't doing worse, certainly.

Mr. SABO. Where the pressure point should be is with the local office?

Mr. WEICHER. I think that is the first place, because the local office should know what is happening very specifically. There are 70 local offices and a local problem ought to be something that the local office would know about in the first instance.

Mr. SABO. Thank you.

Mr. HERGER. Thank you. That concludes our first round. Are there any other members that would like to inquire with follow-up questions? [No response.]

With that, this committee will recess for lunch and reconvene at 2 p.m. to receive testimony from the Secretary of HUD, Mr. Cisneros. Thank you very much.

[Recess.]

Chairman KASICH. The committee will come to order.

I want to welcome the Secretary here today. I will say that he is clearly one of the most energetic and hard-working public servants we have in this city. I know that he has made an effort to visit countless Members of both sides of the aisle in trying to explain what he has in his program. As most people will say, he is just a very impressive salesperson for the things that he believes in, and I happen to agree with that. You, Mr. Secretary, put a lot of energy and burn a lot of energy up trying to sell what you believe in, and you and I, for sure, have that in common.

This is a big job you have, and, frankly, we were talking yesterday to the witnesses and a little bit today. There is a problem in HUD that has been essentially not dealt with effectively for a long time. I think it would be real easy to come in and pick on you for X, Y, and Z, but I don't think that would necessarily be very fair, because you inherited a very big, difficult assignment.

I believe you are making some progress in terms of—I don't want to give out a grade; that is not fair to you, either. I think you are trying as hard as you possibly can. You have to deal with some political realities that restrain some of what you would probably like to do. But I think you are moving in the right direction.

I have a lot of concerns about a number of the programs. As you can imagine, I am very concerned about the multifamily program. I am concerned about the mark-to-market program. I am concerned about additional funding for new public housing construction, which kind of flies, in a way, in the face of what you want to do with vouchers and certificates, which I think is positive and follows on with your predecessor on that issue.

But this is a difficult problem that we have to stare square in the eye. I would guess that the mark-to-market program you have,

which I don't happen to agree with, however, is an intellectually honest effort to begin to deal with a lot of the problems that we have in HUD, and they are extremely difficult.

I think it is just important that, as we go through this, we work together as much as we possibly can. There are going to be some hits that we are all going to suffer on this thing when it comes to trying to get good policy going for housing. It is very, very difficult and very challenging.

I want to welcome you here today. I look forward to your testimony.

Mr. Sabo?

Mr. SABO. Thank you, Mr. Chairman.

Mr. Secretary, welcome. It has been a pleasure working with you. You are doing a great job. HUD is one of the most important agencies we have. It deals with the day-to-day lives of millions of Americans. It deals with the fundamental problem of decent housing for Americans. We made progress, but there are still millions of Americans who don't have decent housing that they can afford in our country, and we need to continue to work at that problem. I am concerned when I hear of proposals that would move us backwards rather than forwards in dealing with that fundamental problem as we try to restructure HUD.

I have had a longtime interest in housing programs. My observation, since coming here in the late 1970's, I thought HUD was working reasonably well. I thought it went, then, in the 1980's, through a period of real mismanagement, and then a period of nonmanagement. You have begun to turn that around in making HUD programs work, to break through that bureaucracy so decisions can be made. I really compliment you for that.

I have to say that I have some concerns as we move to increased vouchers that we not forget about new construction. My observation from my community is that there still is a need for new construction of low- and moderate-income housing, not necessarily in areas where all the vouchers go today.

One of the fundamental problems we have in the urban core and in inner-ring suburbs is that that is where all the concentration of both public housing is, that is where the concentration of market rate housing is that lower- and moderate-income people can either buy or can use with their vouchers. Other communities have effectively zoned out any capacity for people to either buy or rent in their communities. This causes immense distortions.

I think that has to continue to be a concern of HUD. I, frankly, think it should also be a concern to the Department of Transportation and some other agencies, probably EPA, as we hand out sewer grants. But that remains a very fundamental problem in my urban area and, I suspect, in others around the country.

I look forward to your testimony and wish you well in what I think is an endeavor you are undertaking to make HUD work more efficiently and more responsibly so we can better serve the needs of millions of Americans.

I also have to apologize. I probably will have to leave for a markup in an appropriations subcommittee before you finish the hearing today, but welcome.

STATEMENT OF THE HONORABLE HENRY G. CISNEROS, SECRETARY, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT; ACCOMPANIED BY BRUCE KATZ, CHIEF OF STAFF; HELEN DUNLAP, SECRETARY FOR MULTIFAMILY HOUSING; AND MICHAEL STEGMAN, ASSISTANT SECRETARY FOR POLICY DEVELOPMENT AND RESEARCH

Mr. CISNEROS. Mr. Chairman, thank you very much, Congressman Sabo. Thank you for inviting us to testify before you and the Budget Committee.

I am joined today by the Assistant Secretary for Policy at HUD, Mr. Mike Stegman, to my right, and the Chief of Staff of the Department, Bruce Katz, who is standing to my left and will assist with these charts.

You, hopefully, by now, have in front of you a set of the charts which are going to be turned here. If you don't, we will try to make sure that you get them, because it will assist you in walking through this presentation, given the distances involved in this room to these tables.

I welcome this series of hearings on the Department of Housing and Urban Development. They come at a critical time in HUD's history, a moment when a confluence of events is driving what promises to be the most far-reaching reform of Federal housing and urban policy since the creation of the Department, certainly, and farther back than that.

Our decisions will affect whether or not some of the most economically vulnerable households in our society will be able to remain secure and remain in decent, affordable housing.

To add even greater urgency to this discussion, at this very moment, the House Appropriations Subcommittee on VA–HUD is considering a recision package that would cut an estimated $7 billion in HUD funds appropriated for this and prior fiscal years. HUD's contribution will run anywhere from one-third to, perhaps, one-half of the total proposed recisions for the Federal Government.

I have written a letter to Chairman Lewis of that subcommittee today detailing what we estimate are the costs, in human terms, of the proposed recisions. They are proposing, we understand, recisions of upwards of $500 million in homeless funding, which would prevent over 30,000 homeless families from moving to transitional or permanent housing.

They are proposing recisions of upwards of $400 million in funding for preservation of the assisted stock, which will displace, of necessity, 27,000 residents from affordable housing as owners try to convert housing to luxury apartments.

And, recisions of something approaching $500 million in community development block grant funds, which will work a particular hardship in disaster-stricken areas such as the floods in the Midwest and the Southeast, which would be particularly ironic if it is victims from the floods who have to give up funds due them in order to create space for dealing with the victims of the California earthquake.

In many cases, these funds are funds that nonprofits have competed for and have already been awarded and that communities and States have been allocated and have banked upon. For example, in the case of the community development block grant funds,

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we have already allocated the first two quarters of funding, so the recisions now being considered have to come deeply out of those communities who were to come in the third and fourth quarter of the fiscal year. The impact of the package is severe.

But that is another subcommittee's work, another place today here in this Capitol.

What it does allow me to do, however, is to emphasize the vulnerability of the population that HUD uniquely serves. We serve approximately 4.7 million households who currently receive HUD housing assistance. As the attached chart illustrates, 35 percent of all subsidized households are elderly and another 10 percent are persons who are disabled, so almost half, 45 percent of the people we assist, are elderly or disabled.

The median income of all assisted households is less than $8,000 a year, and for families in public housing, it is under $6,100 a year. Most households who receive housing assistance would have great difficulty finding affordable housing without government assistance, and, therefore, they live on the edge of what could very well be homelessness.

The need for housing assistance has continued to mount, even during periods of economic recovery. As the attached chart illustrates, the number of very low-income renters paying more than 50 percent of income for rent—now, keep in mind, experts say that rental payments should not exceed, for the average family, about 30 percent of income—the average number exceeding 50 percent of income jumped 700,000 between 1989 and 1993. Those numbers now total about 5.6 million American families, more than the total number of families we help who are eligible but who do not get help.

The dismantling of HUD, as some have suggested, would risk Federal abandonment of low-income housing needs and other important national concerns. Spinning off the responsibilities of HUD to other departments would not only lose the necessary coordination and synergy between programs, but simply assign them to other bureaucracies that would not have had the attendant experience to actually reinvent the programs.

We still need HUD, Mr. Chairman and members of this committee. In fact, I would argue, given the economic conditions in many parts of America, we need HUD now more than ever, but we need a radically changed HUD, and that is why we proposed changes in the way the Department is structured and operates.

Our Reinvention Blueprint has three components. I will describe those. But I want to say just a quick word about our 1996 budget and how reinvention interplays with it.

The fiscal 1996 budget basically freezes budget authority for the agency's programs at $25.7 billion and increases outlays by $800 million to $31.8 billion. As I will explain later, almost 90 percent of our outlay increase is due to prior-year commitments and does not reflect spending from new activity. That is a critically important aspect of the HUD budget, is how much of it is driven by prior-year commitments.

Let me quickly describe the three-part reinvention that the Department has undertaken. The first part, and I apologize for the fact that the distance here is so great that you probably will not

be able to see from this chart—I will move through these quickly—the first chart describes how we get from 60 HUD programs to 8 in our first year of reinvention, and then, eventually, 3.

The key changes or funds will be the creation of an affordable housing fund, which will allow the Department to consolidate the HOME program, elderly programs, and disabled programs into one large affordable housing fund.

Another consolidation is the creation of a community opportunity performance fund, which takes the existing community development block grant program and makes that into one large fund by consolidating a host of other urban programs. In each case, this is not just block grants but it is an attempt to capture the spirit that we discern from this new Congress of performance grants, where communities are given incentives to perform, not sanctions, not heavy oversight, but incentives, and then rewarded with additional funds if they are able to perform.

The first year of our reinvention also groups up all of our homeless programs, the so-called McKinney programs, and consolidates those into one major homeless assistance performance fund. Our programs for persons with AIDS are consolidated, and that accounts for the largest piece of our reinvention, taking these major funds and putting them together.

The second large piece of HUD's reinvention, perhaps the most far-reaching, certainly the most controversial, the one that will touch most people's lives and that most people are most worried about, the one where we have to take the greatest leap of faith that the system can change, is the transformation of public housing.

We will, for the first time in 60 years, provide public housing residents the same privileges that other Americans have. Instead of being the only Americans who have to take a unit because that is all that is available, come off the waiting list after being 3 years on the waiting list and take whatever is vacant at the time, no matter what the neighborhood, no matter what the conditions, no matter what the safety environment, it is what they have to take, we will follow the advice of many Americans who believe that choice really does create market disciplines and give residents a certificate so that they can make the decision as to where they will live, but also inherently put pressure on the public housing authorities to perform.

Heretofore, we have a command and control system where we fund the housing authorities, whether or not they perform or not. We dare not take the money away, because while it might hurt a few public housing executives, it hurts a lot of people. So we fund them, no matter what the conditions of safety, no matter what the conditions of maintenance. Under this new system, we bypass the housing authorities and fund people with certificates and they make the decision as to whether the housing authority warrants their business or not.

This is a process that will take several years to work through. We begin by consolidating our public housing programs into two big funds. We go, literally, from two dozen public housing programs to two, one for capital assistance and one for operating subsidies. We deregulate all 3,400 housing authorities, focusing our attentions on the worst.

And, we accelerate the demolition of the worst developments. You will see on the next chart plans already underway this year for the demolition of some of the most infamous public housing developments in the United States. Already this last year, Washington Park Homes in Chicago, North Lincoln Park in Denver, and Lake West in Dallas are en route to demolition.

This is not because we want to eliminate stock; far from it. The whole point of our exercise and the care with which we drafted this is to maintain the public housing stock. The purpose in approaching it this way is not to demolish stock but, rather, to deal with the worst of it so that the best of it has a chance to survive. As I said, our first step is to consolidate the funds, deregulate, and move to demolition.

The mechanism by which we eventually move to vouchers is the creation of a certificate account, a fund that deals with the creation of housing certificates. We take all of the money that now is public housing development, all of the money that goes to public housing authorities for human services programs, all of the funds that go to housing authorities for modernization, and group them up into one large housing certificate fund. You see here almost $8 billion for housing certificates. That will enable people in the outyears of this effort to make the decision as to whether they will stay or whether they will go.

We presently have our plan before the Office of Management and Budget and hope to bring it forward to the Congress within the next 2 weeks. It spells out the details of how this will work. We think we have finally reached a point where we can safely say, because we have structured the transition, because we have given time for housing authorities to improve the stock, that we can safely say that we will not lose massive amounts of stock in this transformation and yet give people maximum choice.

The third piece of our reinvention is the creation of an entrepreneurial FHA corporation. We go from a slow-moving bureaucracy to a streamlined, market-driven, government-owned corporation, an entrepreneurial corporation that will rely, increasingly, on partnerships with well-capitalized, sophisticated financial institutions, including Fannie Mae and Freddie Mac, the Federal Home Loan banks, private mortgage insurance companies, State housing finance agencies. We will work hard to consolidate FHA's programs into two.

Mr. Chairman, I relate these elements of our reinvention with you because they provide the backdrop for our 1996 budget. We worked hard to make the fiscal year 1996 budget relate to this reinvention. In other words, we didn't just trot out a reinvention and then run a parallel track with the budget. We made these things come together. The budget is the first step. The fiscal year 1996 budget is the first step of our reinvention.

So I would like to begin with a chart that just makes a key point: 88 percent of HUD's fiscal year 1996 outlays derive from prior-year commitments. This is because almost all of HUD's programs spend slowly in the first year. This chart describes 88 percent of our annual expenditures or outlays from previous-year commitments.

The second chart is a complicated one to look at unless you have it in front of you, but the green portion of it describes the relative

proportions of those items, salaries and expenses versus public housing subsidies versus community development, in terms of what percentage they are of our budget, but then in terms of how they spend, you can see that our programs inherently spend slowly. The blue at the far end suggests that small percentages of these funds spend slowly, and that is, of course, logical. It takes time to build something. Building something is not the same as spending on services, spending on personnel. It is inherently different.

So, for example, to say that the way to attack HUD is through recisions that deal with previous-year outlays because, somehow, we have been slow in spending and the pipeline is vulnerable is just to say that things that had previously been decided should be built are not going to be built, because it takes 2 and 3 and 4 years to get to the point of getting things built.

There is a lot of confusion, for example, about the terms of section 8 contracts. Questions about the terms of the contracts only affect the budget authority that is needed, but the length of the contract term does not affect outlays. Outlays would be the same if the contract term is 20 years or 1 year.

We are proposing to shorten the terms for renewals and incrementals to 2 years and, ultimately, to 1-year terms. That makes sense from a policy perspective. When we shorten from multiple years, 5 years, say, to 2 years, we take out some of the peaks and valleys in our budgetary pattern. Program participants are not affected by the shortening of terms, as long as the contracts are reliably renewed.

Shorter terms, as I say, make sense from a budgetary perspective. With the tight caps on both budget authority and outlays, it is unnecessary to tie up large amounts of budget authority in multiyear contracts, so shifting to 2-year certificates generates $21 billion in BA savings over 5 years.

I know that this committee and some of you have questioned whether the proposed BA and outlay savings in HUD's budget are sufficient and whether they are real. This budget reflects a dramatic shift toward policies that will impose market constraints on HUD's support for affordable housing.

For example, we will no longer try to preserve all assisted housing at any cost. In the affected communities, there are better, more efficient alternatives to provide affordable housing for low-income people, so we may well go to a certificate system as opposed to continuing to subsidize units.

Second, we will no longer try to replace all public housing units, regardless of their condition. All we have done by following this blind housing policy is bottle up the poorest of the poor in the worst housing and destroy neighborhoods around them. So, when it makes sense, we will demolish and provide other forms of assistance.

And, importantly, we will stop excessive subsidies to landlords. This means we will no longer subsidize rents in federally assisted housing that are higher than rents for comparable private housing. Right now, we have an awful situation where we are paying rents that are too high because of the history of the project. So our mark-to-market proposal attempts to reduce the debt on these projects and level the payments that will be required.

We are also proposing $476 million in recisions from our fiscal year 1995 budget appropriation, but, obviously, as I have said, some of the recisions now being considered in the appropriations committees are far too stiff.

Substantial savings will also be proposed on the administrative side. Because of our plan, HUD will go from the 13,500 people that it had when I came there 2 years ago to less than 12,000 now to 7,500 in the years that it takes to play out this plan, so about half the size of the Federal employees that it had when I first came 2 years ago, as this plan works through.

As the attached chart illustrates, because of these and other choices, HUD projects a savings of $7 billion in budget authority and $860 million in outlays in 1996, relative to 1995 program levels, adjusted for inflation, and a 5-year savings of $51 billion in budget authority and $13 billion in budget outlays.

These savings come from a variety of sources. On the BA side, they principally come from shortening contract terms. On the outlay side, significant savings will accrue from stopping excessive subsidies to landlords, reducing fair market rent for section 8 certificates, changing admission rules in public and assisted housing to reward work, and the recisions. In addition, the President announced in December more than $800 million in administrative expenses, as we reduce the administrative overload of the Department.

Let me speak directly to the concerns that you have expressed about mark to market. Nowhere is the complexity of HUD's budget more pronounced than in the treatment of the FHA mark to market. There has been some confusion about the substantive intricacies of the proposal. There has been even greater confusion about the budget impact. Let me try to clear up the confusion.

The 1996 budget signals the beginning of a comprehensive effort to transform the older, subsidized inventory into a competitive, market-driven rental stock. As the attached chart illustrates, there are 1.6 million units that were subsidized under older HUD programs. HUD insures the debt on three out of four subsidized properties and then subsidizes the owner's payment of the debt, principally on section 8. We are on both sides of this. We subsidize the buildings from an insurance standpoint and then we pay with section 8, so the landlord makes his payment and never has to default on the insurance.

Rent payments have ballooned over time, as owners received annual adjustments. This has gone on for the last 25 years. They have generally exceeded the increase in operating expenses, so an incredible 75 percent of the older section 8 inventory have rents that exceed fair market rents or market rents in the area. In other words, HUD landlords are getting more from the government in rents than people across the street who are not HUD-assisted.

HUD is, thus, caught in a catch-22. If HUD stops paying the subsidies without adjusting the existing debt, then FHA suffers massive insurance claims because we insure the buildings. If we stop making the subsidies, they can't make their payments, we inherit the properties through foreclosure. The true victims are the residents, of course, because in the public housing, the subsidies are linked to the units, prohibiting the residents from exercising choice.

Some owners participated in the program over the years only to receive the tax benefits and have little interest or ability to continue investing in the properties, so the properties are frequently in bad shape.

We have three ways out of this morass. First, we could stay the course and continue oversubsidizing the inventory, but that would lead to astronomical costs, $64 billion over the remaining mortgage terms without improving the properties or the condition for the residents.

Second, we could turn off the section 8 faucet. Mike's predecessor at HUD, Mr. Weicher, I understand, advocates that course. But, we believe it would result in massive defaults and foreclosures, triggering substantial costs to the government, to the FHA fund. The impact of foreclosures on residents of these buildings, many of whom are elderly and in low-income communities, would be substantial.

So we have set forth a third course. HUD could do what RTC and the FDIC and Freddie Mac and conventional lenders have done for the past 5 to 10 years, mark to market the debt on these properties to reflect their present true economic value, ultimately converting all the subsidies to portable certificates that support families living, but not in those projects. Residents will, thus, be protected, given greater choice, and the Federal Government's credibility in the housing market will be retained.

From a budget perspective, mark to market will mean fewer FHA claims than a more draconian termination of subsidies overnight, and would also save substantial section 8 rental subsidies as the mortgage payments are ratcheted down. It is a budget saver to go this route. Not only do we not suffer the loss of FHA from the FHA fund, but we have mark to market the cost of the properties, reduced the rent payments, and saved money out of section 8, as well.

As the attached chart illustrates, mark to market will have budget impacts on both the discretionary and mandatory sides. On the discretionary side, the budget savings of $1.7 billion in outlays over 5 years as rental assistance to owners is reduced to reflect lower debt service. On the mandatory side, it would be increased costs through partial payments of claims and additional rehabilitation expenditures. We fully expect, Mr. Chairman, that savings from our program reforms will be sufficient to offset the greater costs that I have identified.

Why? First, we are recommending changes to the current property disposition law that will allow properties to be sold on an expedited basis. That means fewer holding costs for HUD, which, since 1989, became one of the largest owners of troubled real estate in the country.

Second, HUD has a classic choice with most of the older subsidized inventory. Either pay a little now or a lot later, as owners ultimately default after years of disinvestment.

I realize that the budget, our budget, does not assign precise saving estimates to these program reforms. We are using the improved financial information that we received from owners over the past 2 years to generate various assumptions about likely owner behavior.

I know one of the traditional raps on HUD is that we don't know enough about our inventory. People say all the time, you don't even know what you have. In fact, we have financial information, good financial information, on 92 percent of the stock, and we know a lot about the remainder. We just don't have the updated financial information on those.

The bottom line is that mark to market is the right thing to do. You have my personal assurance that HUD will deliver full justifications to this committee so that you can proceed with action on the fiscal year 1996 budget within days.

In conclusion, the fiscal 1996 budget represents fundamental change at HUD. We have not changed our mission. We believe it is appropriate for the Federal Government to be involved in housing and that there needs to be a Department of Housing and Urban Development. Although our budget is an important step toward a new HUD, a HUD that is customer oriented, performance driven, more responsive to local needs, our ultimate goal remains the same, to help the American people create communities of opportunity.

The 1996 budget recommits HUD to our priorities, the priorities we have stated from day one, to reduce homelessness, to transform public housing, to create affordable housing and home ownership, to reduce discrimination and be the voice for open housing, fair housing, and to focus on communities.

The country needs a Federal commitment to communities, to its cities, to affordable housing to its most vulnerable people. The nation, at this time, must reassure its cities and their citizens that it remains committed to their role in America's future.

The HUD reinvention effort is an attempt to do that, and our 1996 budget is an attempt to set out the first step on a massive reinvention of the Department.

Mr. Chairman, I look forward to your questions and those of members of the committee.

[The prepared statement of Secretary Cisneros follows:]

PREPARED STATEMENT OF HON. HENRY G. CISNEROS, SECRETARY, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Chairman Kasich, thank you for inviting me to testify before you and the Budget Committee. We have enjoyed a positive working relationship with Congressman Sabo during his tenure as chairman, and I look forward to a developing a good working with you as chairman, as we address the housing and community development issues that are of such vital importance to the American people.

I welcome this opportunity to discuss these issues with you and the committee members as we discuss the successes and remaining challenges of HUD's mission.

The most severe challenge is the challenge to our national commitment to fulfill HUD's mission. There are people here on Capitol Hill calling for the dismantlement of HUD. I take these calls very seriously.

Today, HUD is literally fighting for its life. But we are not fighting to preserve a bureaucracy. We are not fighting for an institution. We are not even fighting for programs. We are fighting to preserve a national commitment to the economic health and social viability of our nation's urban centers.

We are fighting to preserve a vital mission: promoting the business growth, the job expansion, and the increased opportunities for affordable housing and home ownership that poor people and low- and moderate-income working families in economically distressed communities must have to lift themselves to better lives.

No other Federal department or agency pursues this mission today. It is truly unique to HUD. And if HUD were to be dismantled, this mission would truly be lost. For the sake of our nation's future, this must not happen.

Mr. Chairman, the stakes of this debate are not purely financial. The outcomes of our decisions will affect whether or not some of the most economically vulnerable households in our society will be able to secure and remain in decent, affordable housing. Approximately 4.7 million households currently receive HUD housing assistance. We must not forget that approximately 35 percent of all subsidized households are elderly and another 10 percent are disabled. Another 45 percent are households with children, mostly single-parent families.

The median income of all assisted households is less than $8,000 a year, and for families in public housing it is under $6,100. Most households who receive housing assistance would have great difficulty finding decent affordable housing in the private market without government assistance. Indeed, without such aid, many of these households would be at serious risk of becoming homeless.

The need for housing assistance has continued to mount, even during periods of economic recovery. In 1990, your committee first directed the Department to prepare an annual report documenting this Nation's "worst-case" housing needs—those households with incomes of less than 50 percent of the area median income who pay more than half their incomes for rent and utilities or who live in seriously substandard housing.

We have recently completed preliminary analysis of 1993 American Housing Survey data, the most current data available, and found that 5.6 million households had worst-case housing needs—an increase of nearly 700,000 since 1989. The overwhelming problem suffered by these households is affordability: 4 out of 5 households with worst case needs in 1993 lived in adequate, uncrowded housing, but paid more than half their incomes for rent.

The bottom line is that policy changes affecting HUD can have profound consequences both in terms of housing opportunities for millions of low-income families and on the extent to which the assisted housing inventory continues to serve a growing national need.

But HUD must change if its mission is to be preserved, because the old HUD was not serving its mission well. When I came to HUD 2 years ago, I found a department that was more interested in bureaucratic process than it was in results. I found a department that was committed to the perpetuation of programs that no longer worked. I found a department that was distrustful of local ideas, of local initiatives.

Mr. Chairman, President Clinton knows, as you and this committee and I know, the conditions I found could not further the mission of the department. HUD had to change.

President Clinton made a commitment to reinvent government, to make it more responsive to the needs of the American people. He knows, as you and this committee and the Congress know, that people want government off their back, but on their side. He's working to make government better serve the American people. And that's what he asked me to do at HUD.

With the President's support, we set out to change HUD. We eliminated an entire layer of regional bureaucracy and pushed more decisionmaking authority out to our field offices to make the department more responsive to local needs. We streamlined programs and cut red tape, to give local communities more flexibility to solve their own problems.

We re-energized the Federal Housing Administration. In 1994, FHA had the second-best year in its 60-year history, ensuring 1.3 million home loans, including 450,000 for first-time buyers.

We began working with public housing authorities across the country to turn around this nation's most distressed public housing—and the results of this work are starting to show, as old, deteriorating buildings come down in places like Chicago and Dallas.

For 2 years, we have been steadily changing the way HUD does business. Now we are dramatically accelerating the pace of change at HUD.

First, we have proposed to consolidate 60 separately funded, major programs into three broad, flexible funds by fiscal 1998:

Housing Certificates for Families and Individuals, to provide direct housing assistance—based on fair market rents—to low-income people;

An Affordable Housing Fund, to support development and rehabilitation of affordable housing; and

A Community Opportunity Fund, to stimulate community economic revitalization.

This consolidation will sweep away the clutter of separate application procedures, rules and regulations that accumulated at HUD over the last 30 years, as programs were piled on top of programs. And we will free cities and states to solve their own housing and economic development problems in their own ways.

Certain conditions would still apply to the use of these funds: adherence to income-targeting rules; compliance with fair housing laws; attention to vulnerable segments of the population—the homeless, people with disabilities or HIV/AIDS, and the frail elderly; emphasis on transitions to economic independence and home ownership in program design and implementation; and involvement of community-based organizations. But localities and states would have wide flexibility within these broad conditions.

They will also have a powerful incentive to put performance ahead of process, just as we are doing. Our new funds will be performance-based. That means cities and states that produce real, tangible results for the people and communities who need our help today * * * more affordable housing, expanded home ownership, business growth, increased job opportunities * * * those localities and states will get bonuses—more resources and increased flexibility. Cities and states that do not perform will not get extra funds—and in extreme cases, they could face cuts. We are building serious market disciplines into these funds.

Second, we've proposed to phase out direct subsidies to public housing authorities. Instead of subsidizing buildings and bureaucracies, HUD would provide direct assistance to residents. They would be able to make their own choices about where they live, and housing authorities would have to compete with other housing providers for their business. When this transition is complete, public housing will be indistinguishable from conventional housing, and it will be a true asset to our communities.

Third, we've proposed to transform the Federal Housing Administration into an entrepreneurial, government-owned corporation, which will work much more effectively with the private market to expand home ownership and to develop more affordable rental housing.

In very broad brush strokes, that is our reinvention.

HUD's 1996 budget translates our reinvention into concrete action. It is a vehicle for fundamental change at the Department of Housing and Urban Development. Our budget:

Launches our reinvention blueprint by starting the process to give low-income people the chance to make real choices about where they live, providing communities the resources to address local needs, and expanding home ownership opportunities for low-, moderate-income and middle-class working families;

Delivers on the President's commitment to communities by strengthening the capacity of cities and states to develop and implement their own initiatives. Through performance partnerships, for instance, cities will see a 27-percent increase in funds actually available directly to them to expand affordable housing, promote business development and increase job opportunities;

Slashes HUD's bureaucracy and gets HUD out of the business of prescribing solutions and back to the business of supporting local initiatives; and

Reflects tough choices we have had to make in balancing our desire to fund the consolidated programs at fiscal 1995 levels with the need to meet tight spending caps.

This budget achieves all these objectives within the constraints of the very tight fiscal environment in which we operate today. We have been able to maintain HUD spending at virtually the same level as fiscal 1995: $25.7 billion in budget authority and $31.8 billion in outlays. The critical difference is in how these resources will be deployed. That is where reinvention—and some very tough decisions—come in.

It is a new day at HUD. The American people demand a Federal Government that works better, makes the best use of their tax dollars, and supports local initiatives rather than handing down edicts from Washington. Our fiscal 1996 budget gives the American people a new HUD that will more efficiently meet the complex needs of communities.

HUD's reinvention carries out President Clinton's directive to consolidate categorical Federal programs into performance partnerships that devolve initiative and decisionmaking authority to localities and states.

Here's how the funding levels we propose for 1996 will launch the program consolidation that is fundamental to HUD's reinvention.

AFFORDABLE HOUSING PERFORMANCE FUND

We propose $3.34 billion for the Affordable Housing Performance Fund. This Fund consolidates current grants for housing production and rehabilitation, including home ownership initiatives, into a single, flexible program: 90 percent of these funds would be provided to localities and states on a formula basis, with a national set-aside for Native Americans; 10 percent would be held back to reward superior performance.

Affordable housing funds would be allocated to states, cities, and urban counties using the current HOME formula: 60 percent to local jurisdictions and 40 percent to states. We would continue the current set-aside for community housing development organizations.

COMMUNITY OPPORTUNITY PERFORMANCE FUND

Our 1996 Budget proposes $4.85 billion to consolidate 14 current HUD grants for community economic development into a single Community Opportunity Performance Fund.

This program would build on the highly successful and popular Community Development Block Grant (CDBG) program by providing localities and states with the flexibility to fund a wide range of community-based economic development and revitalization activities now served by independent programs.

Formula funds would be allocated using the current CDBG formula: 70 percent to large cities and counties and 30 percent to states with a set-aside for Indian Tribes. Superior performers would compete for a 5-percent bonus pool.

HOMELESS ASSISTANCE PERFORMANCE FUND

The budget reflects our commitment to vulnerable populations. We have proposed $1.12 billion to create a single Homeless Assistance Performance Fund to provide flexible support on a combined formula/performance basis to States, local governments, nonprofit organizations, and Indian tribes.

This new grant program would consolidate the existing HUD McKinney programs into a single Homeless Assistance fund to enable communities to shape a flexible, coordinated "continuum of care" approach to solving homelessness.

HOUSING OPPORTUNITIES FOR PERSONS WITH AIDS

We also propose a 1996 appropriation of $186 million to meet the special housing needs of persons with AIDS. The program allocates funds to grantees based on the incidence of AIDS. Such activities include: housing information and coordination services; short-term supported housing and services; short-term rental assistance; single room occupancy dwellings; and community residences and services.

COMMITMENT TO CITIES AND STATES

What these resources amount to in fiscal year 1996 is a significant commitment from this President and HUD to cities and states.

In 1996, the share of the budget to local and state governments will grow and they will get an increase in funds.

For example, for America's three largest cities alone, the increase in funding for community and economic development totals roughly $325 million.

HOUSING CERTIFICATES FOR FAMILIES AND INDIVIDUALS

The HUD budget proposes $7.67 billion for consolidation of all section 8 rental assistance programs that provide housing assistance to families and individuals.

This consolidation is the first step in a multiyear process toward consolidating all current public housing, assisted housing and rental assistance programs into one fund for tenant-based housing assistance administered at the state and local level. In fiscal year 1996, we would provide 50,000 additional households with new certificates to help them afford rental housing in the private market. This is an increase on top of almost 400,000 certificate renewals.

Our budget and the overall administration budget show a clear commitment to affordable housing. Taken together, our 1996 budget, the Agriculture Department's rural housing programs, and the low-income housing tax credit will produce or rehabilitate new affordable housing units, or provide subsidies for more than 500,000 additional families and individuals.

TRANSFORMING PUBLIC HOUSING

We propose transforming the current public housing system by giving residents market choice in the search for affordable housing, by ending the monopoly of housing authorities over Federal housing resources, and by accelerating the demolition of uninhabitable or non-viable public housing developments.

Beginning this year, all public housing programs will be consolidated into two accounts for capital expenditures and operations; a performance-based system would be instituted through deregulation of more than 3,300 well-performing housing authorities; steps would be taken to improve the operations of more than 100 severely

troubled authorities; and thousands of severely deteriorated units would be demolished and replaced either with tenant-based certificates or small-scale, scattered site housing.

Two funds would be created this year.

PUBLIC AND INDIAN HOUSING OPERATION PERFORMANCE FUND

Our fiscal year 1996 Budget proposes $3.2 billion for a consolidated public housing operating grants program.

This proposal would allocate most operating funds for public housing authority operation according to the existing performance funding formula. However, $172 million in bonus funding would be awarded to support PHA's demonstrating rapid progress toward the new system of assistance.

We also propose changing tenant admission rules to give greater preference to families that are either working or enrolled in job training or education programs.

PUBLIC AND INDIAN HOUSING CAPITAL PERFORMANCE FUND

We propose $5.17 billion to consolidate all current public housing capital programs into a single Public and Indian Housing Capital Performance Fund. This Fund would provide Federal resources to rehabilitate and restore viable public housing in need of modernization, demolish uninhabitable and non-viable public housing projects, and construct replacement housing where feasible.

THE FHA CORPORATION

FHA's bureaucratic structure and rules impede sound business practice, and its one-size-fits-all products cannot be tailored to local needs or specialized markets. To operate effectively, FHA must change dramatically, relying more on market incentives and private sector partners to boost housing production and increase home ownership.

The reinvention of FHA will create a government-owned, market-driven enterprise that would use Federal credit enhancement to finance expanded-home ownership opportunities and the development of affordable rental housing. This is good news for middle-income and lower-income people, minorities and new immigrants, people the private market does not always serve.

The new FHA corporation would consolidate FHA's 29 existing insurance programs into broad single-family and multifamily insurance authorities.

The new FHA would rely increasingly on partnerships with well-capitalized, sophisticated financial institutions, including Fannie Mae and Freddie Mac, the Federal Home Loan Banks, private mortgage insurance companies, state and local housing finance agencies, and community-based organizations, to design a variety of products that meet market needs and share risk.

Performance goals would be set to ensure the new FHA's accountability on such measures as meeting the needs of underserved populations, budget issues, and financial performance.

RESTRUCTURING MULTIFAMILY HOUSING

Reinvention will permit the restructuring of debt on FHA's existing portfolio of insured multifamily properties, which will achieve meaningful cost savings, enhance housing quality, and allow properties to compete in the marketplace for renters holding tenant-based assistance.

Property disposition and asset management procedures will be streamlined in a way that is cost-effective, while protecting tenants and ultimately reducing the government's role.

We would revise the costly 1990 preservation law to narrow the universe of properties that are eligible for Federal subsidies.

Many older insured and assisted properties lack the necessary resources to be maintained as quality housing. Many of these projects have been sheltered from the conventional rental market, and the excessive rents they require would not permit them to compete in the market. Rather than continuing to artificially prop up these properties with more rental assistance, it is better and less expensive to establish these true market value. As part of this approach, debt service on some properties will be reduced to a level that will allow them to compete in the rental market without relying on project-based rental assistance.

FAIR HOUSING

The reinvention of HUD and spending reductions will not come at the expense of the Department's responsibility to enforce fair housing and equal opportunity. Ac-

cess to housing must be made a reality for all Americans. The availability of home ownership opportunities and rental housing free from discriminatory impediments are essential to strengthening America's communities.

The Budget provides $45 million to expand support for two existing programs—the Fair Housing Initiative Program (FHIP) and the Fair Housing Assistance Program (FHAP)—that enable HUD, working with nonprofit groups and state and local governments, to aggressively enforce the Nation's fair housing laws. This funding will enable the Department to assist an increasing number of state and local agencies who administer fair housing laws that have been certified as "substantially equivalent" to the Fair Housing Act.

TOUGH CHOICES

What we are proposing is radical change, with the goal of moving resources to communities and enabling communities to do more with them. Change of such magnitude is difficult at any time; at this time, when Federal spending is frozen, the challenge is particularly difficult. Fiscal constraints and the desire to reduce Federal spending force a series of trade-offs. Reductions and reforms in one area are used to sustain funding levels in another.

The tough choices we have made are based upon the same principles we set forth in our Reinvention Blueprints:

Maximum flexibility should be in the hands of decisionmakers at the neighborhood, local and state levels; and

Low- and moderate-income families should have greater power to make decisions about their lives, and government should support their quest for self-sufficiency. In other words, the focus is people over projects.

The very character of HUD needs to change if the reinvention of our policies and programs is to succeed. HUD must become more entrepreneurial, a true partner for change in communities.

The tough choices we have made balancing our desire to fund the consolidated programs at fiscal 1995 levels with the need to meet tight spending caps.

We will no longer try to preserve all assisted housing at any cost. In the affected communities, there are better, more efficient alternatives to providing affordable housing for low-income people. We will no longer try to replace all public housing units regardless of their condition. All we have done by following this blind housing policy is to bottle up the poorest of the poor in these places and destroy the neighborhoods around them.

We will stop excessive subsidies to landlords. This means we will no longer subsidize rents in federally assisted housing that are higher than rents for comparable private housing. There is no reason why assisted-housing landlords should collect more in rent than landlords who operate without taxpayer dollars.

We propose reducing the term of section 8 assistance to low-income families from 5 years to 2 years.

Some of these choices reflect a dramatic shift toward policies that will impose market constraints on HUD's support for affordable housing.

Substantial savings will also be proposed on the administrative side. The consolidation of HUD programs into three performance-based funds and the move toward an FHA corporation will obviate the need for the current numbers of HUD staff and field offices. What HUD staff do, how they do it, and where they do it will be inexorably altered by this ambitious restructuring.

In the first 2 years of this administration, we have already cut the department's work force from 13,500 to about 12,000 employees. Over the next 5 years, we will cut deeper, shrinking HUD to about 7,500 employees.

Thus, as the President announced last month, more than $800 million in administrative expenses alone will be saved over the next 5 years.

We propose $476 million in rescissions from our fiscal 1995 budget appropriation, including $100 million for a never implemented public housing management reform proposal, $80 million that is not needed due to a backlog of unused funding for a private housing lead-based paint hazards removal program, and $150 million for a preservation/prepayment program that HUD believes is too complex and too generous to some landlords.

Because of these and other tough choices, HUD projects a savings of $7.6 billion in budget authority and $860 million in outlays for fiscal 1996, relative to fiscal 1995 program levels after adjusting for inflation; and a 5-year savings of $51 million in budget authority and $13 million in budget outlays.

CONCLUSION

These and other tough choices are absolutely necessary for us to complete HUD's reinvention and do a better job of fulfilling our mission. They make possible the 1996 budget, which enables the creation of new opportunities for partnerships among HUD, local and state governments, the private sector, and community-based organizations.

This budget represents fundamental change at the Department of Housing and Urban Development. But we have not changed our mission or our ideals. Although our budget is an important step toward a new HUD that is customer-oriented, performance-driven, and more responsive to local needs, our ultimate goal remains the same: to help the American people create communities of opportunity.

The 1996 budget recommits HUD to the priorities we have held since day one: strengthening competitive cities and revitalizing neighborhoods; expanding home ownership and affordable rental opportunity; reducing homelessness; transforming public housing; opening housing markets; and managing for performance and results.

The country needs a Federal commitment to communities, to its cities, to affordable housing, to local economic development, and to the housing needs of the poorest and most vulnerable citizens. The nation at this time in history must reassure its cities and their citizens that it remains committed to their role in America's future. HUD's reinvention and our 1996 budget reflect that commitment.

Now, Mr. Chairman, I'll be happy to answer any questions you and the committee members may have and discuss with you the successes and challenges in fulfilling the mission of the U.S. Department of Housing and Urban Development.

Chairman KASICH. Thank you, Mr. Secretary.

First of all, in a question about the recisions, are the recisions essentially restoring the funding levels to the President's requested level in his budget?

Mr. CISNEROS. In some cases, the recisions go to carryover funds. About $4 billion of the $7 billion is carryover funds that appear to be available because they are a pipeline, but it is a pipeline, as I have described, that simply takes a while to move through. We have worked hard over the last 2 years to push the money through the pipeline, but where we are talking about the building of new units, it is architectural and site acquisition and so forth.

The other half of the proposed recision does return to 1995-requested levels. That was the administration's position last year. But after the Congress voted the money, effective October 1, and it became the start of the new fiscal year, communities read the budget and we communicated to them what was the law at that time, that X sum of money would be available in CDBG's.

Chairman KASICH. So in other words, what we are rescinding is a big chunk of what Congress added to, in terms of what the President requested. The President requested X number of dollars. Congress bumped up the level. What the new Congress has done is to say that we are going to go with the level that the President wanted.

Mr. CISNEROS. That is the Washington perspective. The community perspective would be that money they had already budgeted and planned for, because it was passed by the Congress of the United States, is now going to be removed, and it has an uneven effect, because some communities were able to get the money in the first and second quarter and others are waiting for the third and fourth quarter. The recisions will have an uneven effect across the country, digging deeper into those that didn't get the funding in the first two quarters, for one reason or the other.

Chairman KASICH. I understand that, but the point is that these recisions, in many cases, do not take us below the level of what the

President himself had requested. Your problem is that the communities thought there was more coming.

At least a little bit by implication, Mr. Secretary, there was kind of a statement that these are somehow really wrenching cuts, and they are nothing more than what you had recommended to the President, which the President then recommended to the Congress?

Mr. CISNEROS. Mr. Chairman, as I said, that accounts for half of it. The other half, which is a very substantial sum of money—we are talking $7 billion in recisions from one department.

Chairman KASICH. Yes.

Mr. CISNEROS. I watched the newscast last night and saw my colleagues from the Cabinet decrying $200 million cuts here and $400 million cuts there for weatherization and other things. I sympathize with them. But $7 billion from one department, almost half of the total Federal departmental recision coming from one department.

Yes, in some cases, because it involves the carry-forward funds, communities will not be able to do what they had thought for years they would be able to do, modernize some public housing or build some new development or build some homeless facilities, because the money that was in the pipeline will be wrenched away.

Chairman KASICH. But, of course, in your testimony, you indicate that we need a major reinvention of HUD. What you lay out for us this year is a dramatic change in the previous policies.

Mr. CISNEROS. Yes, sir.

Chairman KASICH. You can't have it both ways, can you? In other words, if you say that the system has been essentially broken and now we are going to get on with a change, shouldn't we get on with the change now and not—let us make the change.

Mr. CISNEROS. Yes, sir, but bear with me. I respect your views and I want to lay this out for you. You agree, you said so in your opening comments, that we ought to be moving toward a voucher system in public housing.

If we move to a voucher system overnight, let us take your home area, Columbus, OH, overnight, people will take those vouchers and leave public housing and we will have huge empty buildings blighting entire neighborhoods and lose that stock of what could be perfectly good housing refurbished. The country loses tens of thousands, hundreds of thousands of units of housing that we badly need.

If we had a few years in transition to modernize the stock with the money for modernization, then, when we go to a voucher system, there is a fair fight. It is a level playing field. There is a choice that some of these units are going to survive. The money that is being talked about for recision is the money that is in the pipeline for modernization, so it cuts our long-term plan. In other words, it pulls the legs out from under the kind of reinvention that I am describing to you. That is one area, just one area.

Chairman KASICH. What we are going to have to work on is trying to take the longer-term policy and integrate it with the shorter-term policy and try to make this thing fit. I think the direction you are going is a positive direction. I think the concern is that you want to head to the vouchers here and we are here, and nobody can quite understand what the bridge is. Now, you say you are

going to give us some more details so we are going to be able to look at it——

Mr. CISNEROS. We have figured that one out. I think we have a way to do it. I think everybody in the system, from congressional leaders to public housing authorities to mayors and Governors are going to recognize that this is a way to do it. Save the stock, as much as possible. Serve the residents, as much as possible. We think there is a way to do that. But, in an era when a giant sweeper comes along and takes away the resources, I don't know that any plan can work under those circumstances.

Chairman KASICH. Let me ask you about the mark-to-market program.

Why don't we go ahead and vote first, and then come back. We will be back shortly, Mr. Secretary.

[Recess.]

Chairman KASICH. There are members who have gone over to vote. Mr. Miller is on his way back. We will let him sit in the chair and run the meeting until the rest of us get back. Then, if you want to, you can chair it, and you might go to yourself or Mr. Brownback for questions, however you want to handle it. We will be back as soon as we can. Let us keep it moving, because the Secretary, I am sure, has a busy schedule.

Mr. MILLER [presiding]. Mr. Secretary, if I may, let me go ahead and proceed with a set of questions that I have.

My concern is the area of regulations, and we started this debate in the House yesterday and we will continue it next week about the heavy regulations brought on by the Federal Government. The message of the election last November 8 was to reduce the size and scope of the Federal Government.

My congressional district represents Sarasota, FL, Bradenton, FL, Sun City, Venice, Port Charlotte. I have the largest number of elderly, of retired people of any congressional district in the country, so I have a very large number of senior citizens who have moved down from, especially the Midwest, to enjoy Florida, to enjoy a way of life that is very important to them, especially in mobile home parks.

My problem is regulations on over-55 housing. It is one of the most absurd sets of regulations that I have seen, and it really has a major impact on my district. I know you have received some 15,000 cards and letters on the issue in your office, also, so it is a very big issue. It is a regulatory issue.

As you are probably aware, it is an issue of—and this is something that was passed before I was in Congress and certainly before you were at HUD—is to require significant facilities and services that are specifically designed for people over age 55. It is just a bureaucratic nightmare.

Mr. CISNEROS. Yes.

Mr. MILLER. You introduced some regulations last summer. You had a hearing last summer in my district, or, actually, it was in Tampa. Ms. Achtenberg came down and did an excellent job, visited a mobile home park in Ellenton, Colony Cove, and also visited some others and was very well received. As I said, she did a good job representing HUD.

Mr. CISNEROS. Right.

Mr. MILLER. She had other hearings elsewhere around the country, apparently, as well. After that, the regulations were changed, and so the new regulations came out. Instead of being 60 pages, they are now 29 pages.

The problem is why in the world we have the regulations in the first place, and when you have senior citizens, as I work with so much in my district, these are the new regulations. I know you can't see this, but the people can do this themselves in the mobile home parks. This affects condominiums, but I am especially concerned about mobile home parks because of the way of life that people have moved in there.

A lot of these parks now are resident owned. Under State law in Florida, if a park gets sold, the residents have the first choice to buy it, so a lot of them are smaller parks owned by the residents. Now they have these new regulations that they are going to receive soon that say, this is how they can do the self-certification.

They check off 10 of the following services and facilities, at least 2 facilities or services in at least 5 of the following categories, including, specifically, at least 2 facilities from category 10 or—these people are going to get confused. There are things like you can check off bingo. That is not a very difficult thing. If you have bingo, you have bingo. People are going to make fun of this thing and are going to get mad at the government.

What they are going to say is, all right, I checked off bingo and I posted it on my bulletin board. I meet the requirements. These people want to do the right thing. They are retired people. They remember World War II. They remember the great depression. They are going to do the right thing.

All of a sudden, they miss bingo 1 month and they are going to have a disgruntled person in their mobile home park who is going to file a complaint with HUD, and then they are going to be afraid that the HUD police are going to come down and say, oh, you didn't offer bingo, or you didn't offer a ping-pong table that has been broken for the last month.

These are regulations that people are tired of. Regulations don't affect just businesses. This is one of the few issues where the owners of parks agree with the residents of mobile home parks. The residents are the ones that are fired up about it because this is a threat to their way of life. This is the reason they moved down to Florida, to my district. Harry Johnson is not here; I know he has them in his district, and throughout Florida. It is a way of life that is being destroyed by government interference.

As much as you are trying to make it better, and, I admit, you are making it better, the core question is, why do we have it? Clay Shaw introduced legislation last year. Why not just accept it, to do away with one sentence? All it does is do away with one sentence. It is in our Contract With America. It is going to be passed by the House and eliminated by April 7, and I believe it is going to go through the Senate.

You would make so many senior citizens happy in Florida by saying, we like the idea. Just get rid of that one sentence and just move on. You don't want to have that harassment on you from the seniors, and the seniors feel you are harassing them. That is part of the cost of government. That is the cost of bureaucracy. That is

why government is too big and people want to see it get out of their lives.

That is just one issue that affects me because I have so many seniors, and I am sure there are other illustrations of bureaucracy and regulation. Let us move on and do the important things that you are more concerned about than this. This is not most important on your agenda. You may not even know much about it.

The whole issue of regulations, and this one specifically, why not just get rid of it?

Mr. CISNEROS. Congressman, unfortunately, I do know a lot about it because we have heard a lot about it over the course of the last couple of years.

Mr. MILLER. Good.

Mr. CISNEROS. The issue is that the 1988 Fair Housing Amendments set out a congressional intent on this issue and it had to do with protection of families with children and setting aside the categorization of what constitutes elderly housing so that we could make an exception and allow elderly housing but not create settings where children could not come in the rest of housing. So it had to define what constitutes elderly housing, where families with children should not be, but then drew a clear line so that families with children could be protected in the rest of housing.

At the time, the realtors and AARP and the Children's Defense Fund and other organizations joined together to strike a compromise and the compromise was the law that passed in 1988. It falls to the executive departments, then, to draft regulations, and the first round of regulations that were drafted were just too overreaching and intrusive and micromanaging.

So you are quite correct. We withdrew the regulations and have limited them in a way that most of the organizations, the interest groups for the elderly and others, agree are more manageable.

The long-term solution, of course, is the one you have suggested, which is to change the law so that the departments, then, don't have to regulate or implement those provisions of the law. I wish we could withdraw it unilaterally, but if we did, then we would be accused by someone else of having laws on the books that we are turning our nose up at.

When I came to the Department, it would seem to me like a basic tenet of civics that if the Congress passes a law, the Department should not decide which they will enforce and which they will not enforce but set about enforcing them as the Congress passed them. If the Congress "unpasses" this law, we will quickly remove the regulations.

But there was some logic to what the Congress did in 1988 and it was a deal struck between advocates of children, advocates of the elderly, realtors' groups, and others to try to get it about right. I think we are close, and I don't know what kind of opposition or support you will engender when you seek to change the law, but my guess is that anytime you have interests on both sides of a question, they have to be balanced, and we are pretty close to what I think is a fair balance.

If we can do a better job in regulating and take some of the burden off you with respect to having to change the law, I would be

happy to sit down with you and your office and find out what further improvements and simplifications we can make.

Mr. MILLER. I go to mobile home parks on Saturdays and talk to them. I was there a couple of weeks ago and had 700 people at one mobile home park in Venice, FL. This past weekend, I had 1,000 people at a town hall meeting. They are upset about this. Why is the government getting in the way of their life? It is just one sentence. You could make a lot of people happy, senior citizens and their children up north and grandchildren, by just saying, hey, I support doing away with this one sentence and stop listening to the inside-the-beltway people——

Mr. CISNEROS. The sentence in the law?

Mr. MILLER. Pardon?

Mr. CISNEROS. You are saying, that sentence in the law, or sentence——

Mr. MILLER. Remove that one sentence in the law.

Mr. CISNEROS. In the law?

Mr. MILLER. The way the regulations used to be is if you had over 80 percent of the people over age 55, you met the requirement, a simple, easy way to make it. But when you start going into significant facilities and services that are specifically designed—bingo is not necessarily specifically designed. How do you get a ping-pong table specifically designed?

Mr. CISNEROS. Right.

Mr. MILLER. Someone could challenge these. Why waste your time on this and upset so many people? Arizona people have that problem, too, and California people. It is just overregulation. All we want to do is remove that one little sentence and go back to the 80 percent of the people are over age 55. That satisfies it, no arguments, no debates, people can move on with their lives and not have to worry about the Federal Government messing around with them.

They don't get it yet in Washington, is the only thing I can say. I wish you could just look at it seriously, about supporting the Shaw language. We are going to pass this in the House, because it is in our contract. I don't think there is going to be any controversy there, and hopefully, it is not going to be a controversial issue in the Senate.

That is just one issue of regulation. There are a lot more, so I would appreciate your further looking into accepting the Shaw language.

Mr. CISNEROS. If you will do your part, which is to change the law, we will gladly do our part with regard to the regulations.

Mr. MILLER. If you would support it, it would make it a lot easier and you would make a lot of friends in Florida, I assure you. Thank you very much.

Mr. Brownback.

Mr. BROWNBACK. Thank you very much, Mr. Chairman. I appreciate that.

Thank you, Mr. Secretary, for coming to the committee today.

Mr. CISNEROS. Yes, Mr. Brownback.

Mr. BROWNBACK. I appreciate meeting with you yesterday and your efforts to reinvent HUD. I have a couple of questions about that. In looking back at past efforts to reinvent HUD, I am sure

you did that, how many did you locate? How many efforts were there since HUD has been created to reinvent the institution?

Mr. CISNEROS. I am sorry, I have not looked at it in that way. There has been sort of steady evolution of the Department, addition of programs, deletion of programs over the years, but I don't know of any sort of generational changes.

The changes that we are proposing are the most sweeping since the creation of FHA 60 years ago, the most sweeping since the creation of public housing 60 years ago, and, certainly, the most sweeping in the core of the Department since it was created in 1965, 30 years ago.

I would just say, this is a sincere effort at trying to make change.

Mr. BROWNBACK. I think it is, but since 1965, we had testimony this morning from two people that you are on the fourth attempt to reinvent HUD since 1965. In 1973, after a wave of scandals, there was an attempt to reinvent HUD. In 1983, President Reagan did a reorganization effort on HUD. In 1989, there was another string of scandals in HUD and there was an effort to reinvent it at that point in time.

According to the testimony this morning, this is the fourth effort since 1965 to reinvent HUD. You wouldn't have any problem with those statements from this morning?

Mr. CISNEROS. Congressman, I would say this. Much of what you have suggested as reorganizations were attempts to get a handle on some particular management problem in the Department, usually generated by a scandal or perhaps even to reform a particular program, like the FHA project-based program, which was the source of scandals.

What we are proposing now is a massive remake of every facet of the Department. We have basically broken the mold and started over. This is a paradigm change, asking fundamental questions. What is the role of housing in the United States, with the U.S. Government in America? What can the Federal Government do? What ought a Federal department do? We restarted the conversation from there.

None of the previous moments that you describe come close to the scale and shaking of the assumptions that this generation of change represents.

Mr. BROWNBACK. You might want to look at some of them to see if they did or didn't, because it strikes me that some of them did try to reinvent it to the nature and extent that you have. My concern is that they all failed to do that, that something was problematic at the core or difficult at the core to be able to continue in HUD. Your own OMB Director, Alice Rivlin, Dr. Rivlin suggests, prior to going to the administration, she questioned whether the Federal Government should have and be in the role of housing.

Have you discussed that with her, and whether or not you agree or disagree together on that?

Mr. CISNEROS. I have read Alice Rivlin's book and writings on the subject, and what she was proposing was a massive swapping of responsibilities between levels of government. Absent that discussion, but simply going forward with the work of a department, she wasn't suggesting that the Federal Government shouldn't be in the business or that America didn't need it. It's just that with a

proper trading of responsibilities, the Federal Government might accept some other duties and other levels of government would accept housing. But it wasn't the discussion that went forward in a vacuum. It was in a spirit of shared and swapped responsibilities.

Mr. BROWNBACK. So would she go further than you would go? Would she go the same distance that you have on reinventing, devolving, bringing in local units of government, privatizing?

Mr. CISNEROS. I believe that, from what I can tell of Alice Rivlin, I can't speak for her, but what I can tell of the discussions that we have had almost weekly during this reinvention process, she thinks we have gone an immense distance. I don't know Alice Rivlin to be a "huggy" person, but I have gotten a lot of hugs from her for the progress we have made on this reinvention. We have made her job easier, I think.

Mr. BROWNBACK. I don't know if she is huggy or not, either. She may be; I don't know. I am new to this town. [Laughter.]

Why not on down the road as far as she would take you, then, in her earlier writings?

Mr. CISNEROS. I think we have gone a long way, Congressman.

Mr. BROWNBACK. You have. Why not the full length?

Mr. CISNEROS. Because I don't know that anyone in America, at this moment, Democrat or Republican, is having the discussion about how the pieces interact, what the Federal Government accepts to let the States be relieved of other responsibilities so that they could accept housing for example. That is the kind of discussion she was having, about shared responsibilities. We are talking here about one department.

Now, when we hear a larger discussion that the Federal Government will relieve the States of all health care or all Medicaid or something and in that place they will take housing, that is a different subject, but that, to be honest about it, is the context in which Alice Rivlin wrote earlier, my recollection of her writings.

Mr. BROWNBACK. Thank you, Mr. Chairman.

Chairman KASICH [presiding]. Let us go back a little bit to this new reinvention. You are such a good salesman. I think your rhetoric kind of goes a little bit farther, Mr. Secretary, than the reality.

Let us talk about the mark to market. First of all, we have a GAO report and an IG study that indicates that the information management systems that you have in HUD, and you inherited this, but, frankly, what they say is you are not in a position to really determine the financial conditions of a lot of these properties.

Now, what you want to do in order to fix this, we have a situation, and if Americans across the country understood this, they would shake their heads and really vote for term limits. They would make it maybe a 2-year term limit for Congress.

We are guaranteeing the mortgages for these properties. The properties are worth less than the mortgages, and we are paying rents that are far in excess, in many cases, of the market rent prices.

Mr. CISNEROS. Correct, 75 percent.

Chairman KASICH. So what you want to do is you want to go to 14,000 units and you want to get into negotiations with them. What you are going to do is you are going to say, we are going to negotiate down the value of these properties and we are going to

pay the lenders a chunk of money and then we are going to say we are whole. We have finally reduced the mortgage rate to the rate of these properties. You are going to get into negotiations. In negotiations, everybody is a loser, to begin with. In the end of a good negotiation, it means no one is happy. That is the definition of negotiation.

But secondly, once you negotiate it down, 14,000 projects—and you don't have a plan to get that done. You can't get it done in a year. You might not get it done in 20 years, who knows. You have 14,000 negotiations, and you don't know the status of these properties. You can't tell what the right number is because you don't know whether they are even viable. Once you negotiate the rates down, you are still going to run the same system.

And do you know what could happen? You, first of all, would pay off the lender, which you can't tell us what that is going to cost because you haven't negotiated the 14,000 properties. Then you keep the thing operating under a section 8 multifamily government-assisted program. We may pour more money into those programs and find out it is still not viable, and then we default on the whole darn thing. That is where Mr. Weicher is coming from this morning.

Why get into this negotiation? Why not just cut our losses and tell the landlords, we are going to pay you the market rent. If the market rents don't carry the day, then we are going to need to start moving to dispose of the property and move to the certificates.

This is a very dangerous concept which would mean we would have to have the fifth reinvention of HUD. Why don't you talk a little bit about how we get that done on a real-time, real case-by-case basis?

Mr. CISNEROS. Congressman, first of all, let me say that we do know more than the stories of the last couple of years would have you believe about the financial condition of the stock.

Chairman KASICH. Would you yield just for 1 second?

Mr. CISNEROS. Yes, sir.

Chairman KASICH. I want to tell you, this is something you got. The fact that you don't know the condition, I can't put the finger on you. You inherited this. It has been ignored for too long.

Go ahead, sir.

Mr. CISNEROS. Let me just say that seated to my left is Helen Dunlap, who has been working in the field of multifamily housing for years in California and who is, literally, one of the Nation's experts and most respected people in this field. She is the person who has helped us design this answer.

But she assures me, and I would like her to speak, if you don't mind, to answer your question directly, that we do know the condition of 92 percent of the portfolio. It wasn't that way when we came 2 years ago, but today, we have good information on 92 percent of the portfolio and good, but not complete information, on the remainder.

Secondly, we will not be doing this through negotiation but independent assessments of the condition of the property, which are not negotiations but stipulations by the Federal Government as to what we will do. We are in the power position on these things.

Finally, we will set timetables that are associated with the renewal timetables between now and the year 2003, so this is not an open-ended proposition that goes on forever.

Finally, let me just say that one has to weigh the alternatives, and we are on both sides of this equation. This is the way this developed, that we are on the insurance side of it, having insured some of the properties as well as paying some of the subsidy. We will get it in one place or the other unless we do this middle course road.

With the proviso that she speaks briefly, would you allow Ms. Dunlap to give you a direct answer?

Chairman KASICH. Yes. Go ahead.

Ms. DUNLAP. Thank you. Let me reiterate just a couple of points. We have financial statements, as of this moment in time for last year, as the Secretary pointed out, for 92 percent of the portfolio. That is up from 60 percent the year before. So when we say we know everything about the properties, we don't, but we certainly know the financial condition by certified financial statement for 92 percent of the portfolio at this point, and the physical——

Chairman KASICH. Is that from the owners?

Ms. DUNLAP. They are from audited independent financial statements, as required by law. They come in from the owners, but they are done by independent CPA's.

We also have a contractor who for the last year-and-a-half, has been further reviewing those financial statements and working with us to do some enforcement work.

The second point that I would clarify is that the intent of this proposal is to do the restructuring of the real estate at the time of the contract expiration, so we don't expect to do it all in 1 year. In fact, the expirations are spread out over the time between now and the year 2010, under legal requirements. The bulk of them are between now and the year 2003. So we are talking about a steady buildup, in which we would expect to do the actual work with independent criteria for restructuring, and both contractors and intermediaries to do the specific reevaluation.

I guess I would close by pointing out, again, that our experience has been that the cost of foreclosure, disinvestment, and property disposition is significantly greater than this proposal. The cost of us holding a piece of property and the time that it takes us to foreclose, given current law, is quite substantial.

Chairman KASICH. I appreciate what you are trying to do, it is just a matter of whether you think something like this can happen. We are now looking at the year 2010 before we get through it and can make a full assessment.

I also wonder about those financial statements. The testimony yesterday, the IG indicated a very serious concern about what they call gross inadequacies in your ability to make these determinations. But what is also interesting is that you also have kind of a rainy day fund. You continue the subsidy for these section 8 housing programs. You say that you want to get out of it, but yet, you still have a pot of money that will be made available to these section 8 multifamily units.

Ms. DUNLAP. Mr. Chairman, I am confused about the last point.

Chairman KASICH. You have a rehabilitation pot that goes——

Ms. DUNLAP. No, it is not a rainy day fund.

Chairman KASICH. It is a continuation of extra money that flows into these units.

Ms. DUNLAP. No, at the time of restructuring. First of all——

Chairman KASICH. Which is when? What year?

Ms. DUNLAP. We would appreciate it if these contracts renewed earlier than the year 2010, but we inherit contracts and the majority of them come up for renewal between now and the year 2003.

Chairman KASICH. But that is precisely why I say, why don't we cut our losses now? Why don't we go to a market-based system now? Why go through negotiations, which it will end up being with 14,000 properties with a financial situation that is labeled in some quarters as grossly inadequate?

It isn't working, folks. It just isn't working. Your idea of going to the vouchers and letting people be able to choose makes great sense, but we have to get there sooner, rather than later, because what we are doing is just carrying on the same business because we are afraid to make a break.

Ms. DUNLAP. Mr. Chairman, I would answer the question in two ways. First of all, the legal obligation of the contract is binding. If the Congress wishes to take action that is contrary to that, it is still a legal contract.

Now your second question is, why, at the termination of that contract, whenever it may be, don't we simply turn off the subsidy going forward from that point, and we have suggested that that is the most costly alternative.

[Technical interruption—microphone off.]

Ms. DUNLAP [continuing]. Which is the legal requirement that currently requires us to continue to raise the rent. We totally agree with you that that particular provision should be removed from the law.

Chairman KASICH. Mrs. Myrick, then Mr. Coyne.

Mrs. MYRICK. Mr. Secretary, thank you for being here and for your time with me yesterday.

Mr. CISNEROS. Yes, ma'am.

Mrs. MYRICK. Did you eliminate any programs? I haven't had time to go over that thoroughly. In your consolidation effort into three, did you eliminate any, or just consolidate everything that you are currently doing?

Mr. CISNEROS. We began with some 240 different——

[Technical interruption—microphone off.]

Chairman KASICH. Thank you, Mr. Secretary.

Mrs. Myrick, why don't you go ahead and start over.

Mrs. MYRICK. Let me rephrase, please. Of the 240 programs that HUD currently has, before you consolidated them, were any of those eliminated, or did you accept the ones that weren't working and just put them into group, eventually down to three?

Mr. CISNEROS. Essentially, what we did was we grouped everything together in the plan of bringing you legislation, the authorizing committees, that would, in the process of consolidation, terminate programs. In other words, they will no longer exist as titles of law. We are asking for a consolidation that will cease their existence. But these are not things we can do alone because they are passed as authorized acts of the U.S. Congress.

Mrs. MYRICK. You said that you had copies of financial statements on the different properties. Would it be possible to get a list of those or copies of those for the committee?

Ms. DUNLAP. We have them for approximately 14,000 pieces of real estate, so they would be rather bulky. Usually, the financial statement itself is proprietary. We can certainly create some kind of a summary information for the committee.

Mrs. MYRICK. If you could, that would be great.

Ms. DUNLAP. Certainly.

Mrs. MYRICK. The other is, you mentioned, Mr. Secretary, being concerned about the $7 billion in cuts that you are going to get.

Chairman KASICH. Mrs. Myrick, do we want them to give us 14,000 statements? Do we want them to work on that?

Mrs. MYRICK. No, a summary.

Chairman KASICH. A summary document? That would be good.

Mrs. MYRICK. Yes, just a summary, not the pieces of paper.

Mr. CISNEROS. We need some moving trucks.

Chairman KASICH. I can see the Secretary with pizza at 11 at night, stapling it together.

Mr. CISNEROS. Or the moving vans showing up at your office, Mr. Chairman. [Laughter.]

Mrs. MYRICK. I think we were on the same wavelength.

When you talked about the fact that some of the moneys are unspent because it takes so long to build projects, according to information that we had received out of the 1993 fund, the 1995 budget, there was something like $2.2 billion in section 8 subsidies that had not been spent. Why is that money not being used on time?

Mr. CISNEROS. Do you care to answer it?

Mr. STEGMAN. Some of the section 8 money is the multiyear contract authority that is not supposed to be spent in this year. It is reserved for the term of the contract.

Mrs. MYRICK. I understand. Why does HUD subsidize vacant housing units in public housing projects with operating subsidies?

Mr. CISNEROS. That is an argument that we have had over the years, but it is essentially because if we didn't subsidize them, then we would have absolutely no hope of bringing them back on-line. The intent is to try to reduce the vacancy rates and to get them reoccupied, but with it goes the capacity of the public housing authorities to try to bring them back on as units.

Mr. STEGMAN. Not all vacant units do receive operating subsidies. The operating subsidy under the current law, operating subsidies are based on a 3-percent vacancy rate. Above that, if they are not part of an approved modernization plan or not formally out of the inventory, they are not included in operating subsidies. But there still are security costs and operating costs in a building that has vacancies in it, and so you can't really not subsidize all of that because there are vacancies. But most of the vacancies are not subsidized.

Mrs. MYRICK. Thank you, Mr. Chairman.

Chairman KASICH. Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Welcome, Mr. Secretary, and thank you for your testimony.

Mr. CISNEROS. Yes, Mr. Coyne.

Mr. COYNE. The Department of Housing and Urban Development, for years, has been operating with the policy of requiring replacement housing for units that have been taken out of service. I assume that is still the current policy of the administration at HUD. How is your restructuring proposal going to impact that?

Mr. CISNEROS. Our restructuring proposal requests congressional leniency, if you will, on the so-called one-for-one replacement. We are asking for the elimination of the one-for-one replacement law because, frankly, one-for-one replacement today makes it impossible to bring units down.

If we had to replace every single unit, let us say, in Pittsburgh, where you have some very troubled developments, Allequippa Terrace, for example, if we were to try to replace every one of 800 units in a development like that, there simply would be no way to do it. There isn't the money to do it. There isn't the land to do it. There isn't the zoning to do it. There isn't the community will, with not-in-my-backyard syndromes at work in neighboring communities and so forth. So what we are saying is people are doomed to live in those conditions because we can never provide replacement housing in hard units.

So by waiving or making more lenient one-for-one replacement, then we can give people certificates, vouchers, come up with other approaches to building units that will allow them to move instead of entrapping people in these worst of developments, because one-for-one replacement is just unattainable.

Mr. COYNE. Thank you.

Chairman KASICH. Mr. Hoke.

Mr. HOKE. Thank you, Mr. Chairman.

Thank you, Mr. Secretary, for coming.

Mr. CISNEROS. Yes, Mr. Hoke.

Mr. HOKE. I want to go back. I would like to understand the system better and how we have gotten into this situation. Most of the problem is the section 8 housing, is that correct?

Mr. CISNEROS. Well, we have a lot of problems. [Laughter.]

The public housing is probably the biggest headache we have in terms of the sense of something wrong in America, but the section 8—and there are sort of three different kinds of section 8. There is section 8 where people get a certificate and can move. That exists today.

There is section 8 tied to private developments, so-called project based. We are not in that business anymore in terms of new units, but we are living with the backlog from the 1970's and the 1980's. Secretary Kemp ended the program because it is that very program that was the most controversial. It is that program——

Mr. HOKE. That is the one that has been abused the most.

Mr. CISNEROS. Yes. What happened was people were giving section 8, which is a precious way to fund a development, it is almost like a guarantee that you are going to make a profit and you are going to get rich as an owner of a building, to friends and influential people and so forth. The story that you saw in today's paper about former Secretary Watt is from that era and that program. It doesn't exist anymore, but we are living with the legacy of the section 8 attached to the units, attached to the buildings and with contracts.

Mr. HOKE. That is the part I would like to understand better. So we have a bunch of section 8 housing that was privately developed?

Mr. CISNEROS. Correct.

Mr. HOKE. The part that I don't understand is, let us assume that the market value is below the outstanding mortgage.

Mr. CISNEROS. Correct.

Mr. HOKE. This is the part that I don't understand, how that came about. Is there not, in the contractual agreement between the owner and HUD, a requirement to maintain those units to certain standards?

Mr. CISNEROS. Let me give you two pieces of the answer, and I will ask Helen to expand, but part of the answer is that, under this provision that she described earlier as section 142, there were requirements that the landlords get assistance increases over the years, again, congressionally inspired, congressionally passed, which made it very lucrative, because they keep getting higher rents and bumps and so forth, irrespective of what is happening.

The other thing is, a lot of people were drawn to the housing market that were not housers. They wanted in for the tax breaks, or they were in other businesses but this was a good investment for them, and so they never really paid attention to the property. You will see, every once in a while, when it is sweeps week for the ratings for television, you will see an easy story, which is to go to one of these developments, talk about what the landlords are making in exorbitant rents, and the condition that the properties are in. It is an easy shot, because, unfortunately, in a small fraction of the developments, these conditions do exist.

Helen.

Ms. DUNLAP. I have just one additional historical note. When the programs were conceived in the late 1960's and throughout the 1970's, their intent was to stimulate the economy and to produce building opportunities as well as affordable housing.

So, as I often describe it, there really are two subsidies in each property, but it is all paid through the rents. There is an affordability subsidy to the tenant and there is what was originally a feasibility subsidy, so that through the rent to the resident, we paid for a property that wouldn't have been built by a private developer at that moment in time, because the cost was higher; the financing was higher. So the rent started out above market. The mortgage started out above what is the private market, and then, as the Secretary has pointed out, it built up over the years.

Now, as to the condition——

Mr. HOKE. Isn't there an opportunity to use the contractual obligation to maintain certain standards as leverage to either rescind our guarantee or make the developer actually improve the units?

Ms. DUNLAP. There is——

Mr. HOKE. Have we done that? What are we doing specifically in that area?

Ms. DUNLAP. There is, and up to the last year, the philosophy of the Department was, essentially, a fear of enforcing those regulatory requirements for two reasons, one, the tenants might be displaced, which isn't true, but was a fear. The second is that when we take enforcement action, we end up with a foreclosed mortgage and a payment against the FHA GI/SRI fund. We have now very

specifically identified that it is worth paying the claims to stop oversubsidizing the property. We are pursuing this situation wherever we have identified it.

Mr. HOKE. When you talk about a foreclosed mortgage, though, isn't there a writeback against the developer or the original borrower if they have been in contravention of their obligations under the agreement?

Ms. DUNLAP. It is very difficult to prove. When we accomplish it, it is usually because we spend significant time in court. We have, on occasion, been successful——

Mr. HOKE. Have we been at all aggressive in pursuing it? My sense is that we are not pursuing it at all.

Ms. DUNLAP. I would suggest to you that that was the case a year ago. We are pursuing it today.

Mr. HOKE. How many cases have we filed?

Ms. DUNLAP. We have 24 folks that we identified last fall who spend all of their time working with taking properties through the disposition process. Each one of them is handling three properties around the country. We call them SWAT teams. Additionally, we have field office staff doing that, as well. In total, we have about 400 properties on watch of one variety or another.

Mr. HOKE. How many of them actually——

Ms. DUNLAP. I can't answer that question. I don't know exactly how many. I have been working on one personally and have spent 100 hours of my time in the last 4 months just to get to the point where we can get the bankruptcy stayed so that we can go after the owner.

Mr. HOKE. I understand that there is a tremendous amount of time involved in this, but one of the ideas of criminal justice is deterrence. One of the ideas of actually making good on these obligations and enforcing them contractually is deterrence. I don't think it would take a whole heck of a lot. Right now, I think the assumption is that you can walk all over HUD.

I assume my time is expired?

Chairman KASICH. It is, and if the gentleman wants to stay, we can come around and you would be more than welcome to continue your questioning.

Mr. CISNEROS. We will try to get you the answer to how many. Bruce, if you could have someone call back and see if Nick has that number. He gave that number to me once and it was a specific number. I just don't want to misstate it.

Mr. HOKE. Thank you.

Chairman KASICH. It will be Mr. Bass and then Mr. Pomeroy.

Mr. BASS. I have no questions.

Chairman KASICH. Mr. Pomeroy.

Mr. POMEROY. Thank you, Mr. Chairman.

Mr. Secretary, at the outset, let me confess that I don't have much of a background in public housing and, therefore, am wrestling with some of the conceptual underpinnings of your proposal. Let us talk about, in particular, the FHA mark to market and buy-down required to accomplish that objective.

As you are aware, Mr. Weicher, this morning, believes that is exactly the wrong thing to do and would prefer to get out of the exposure on those units altogether. Can you help me understand why

you have chosen the route that you have, and can you address the issue of which is the cheaper alternative for taxpayers?

Mr. CISNEROS. Yes, sir. There are essentially three approaches to this. One approach would be to keep doing the same thing, in which we believe the result would be to oversubsidize the inventory. We believe that the cost of that would be some $64 billion over the remaining mortgage terms.

The other approach would be the so-called Weicher strategy, but that would result in massive defaults and foreclosures, triggering substantial costs to the FHA funds. The impact of foreclosures would also be substantial on residents.

Mr. POMEROY. The FHA stands as guarantor on that?

Mr. CISNEROS. Correct. So we believe that the right thing to do is to do what other financial agencies of the government have done—RTC, FDIC, Freddie Mac, and others—which is to mark to market the debt on these properties and reflect the true economic value, converting all the subsidies to portable certificates that support families and no longer projects. Residents, then, would have full protection that they know that they are going to be able to have housing. We believe that is not only the best course from a policy standpoint, but it is the most cost effective from a taxpayer standpoint.

Mr. POMEROY. Generally speaking, it is my experience in the private sector, where you have values collapse, private-sector lenders are really forced to consider analogous circumstances. Do they write the property down or do they take a foreclosure and own it themselves, facing the prospect of substantial loss due to deficiency at the time they try to move the property? Is that essentially what you are wrestling with?

Mr. CISNEROS. Yes, sir, that is essentially it. At this time, the government is in the odd position of being on both sides of the equation. We have a public policy objective which has spurred us to subsidize the families, even as we have an insurance program. If we step on the wrong side of this line, we hurt one side or the other.

As complicated as it sounds, as patient as it must be, the right thing to do is to go through that process of taking these properties, writing them to market, providing portable vouchers for the residents, and lowering the cost to the government, we believe.

Mr. POMEROY. Some of my colleagues in the 103d might be interested in two types of corrections. One is a market correction; the other is an ideological correction, getting government, essentially, out of the business of that type of guarantee. It would seem to me like yours straddles that line, actually moves toward both objectives in a fairly balanced fashion.

Mr. CISNEROS. The one thing we haven't talked about in this particular discussion is that we have something like 1.2 million people in assisted housing. First of all, the government cannot get out of this quickly, because, as Helen Dunlap has said, we do have contracts. These are contractual, legal obligations. People borrowed money, built housing with the government's guarantee that they would be there in an insurance capacity or in a subsidy capacity, so there is that aspect of it.

The other is that we have 1.2 million people that we somehow have to keep from going to the streets, and we think that what we propose is the best way to deal with both of those objectives.

Mr. POMEROY. I believe I can speak for even the most conservative of constituents that I represent in saying that they will want to accomplish the ideological correction at no substantial unnecessarily generated cost as we move that route. That is why your proposal seems to move toward that objective better than any other alternative.

Mr. CISNEROS. Thank you, Mr. Pomeroy.

Mr. Chairman, it strikes me that it might be useful for us to get you a very clear paper, accompanied by some sort of charts that describe what we think to be the principal alternatives that we had to walk through to come to this point and share that with the members of the committee. It might be helpful in sort of laying out the pros and cons, the costs to the taxpayers and so forth of each of the strategies.

Chairman KASICH. That is a good point.

Let me go to Mr. Largent. The gentleman's time is expired. Mr. Allard has agreed not to come back and ask, so with Mr. Largent and then maybe a couple of comments, we will be out of here. Mr. Largent?

Mr. LARGENT. Do you want me to yield?

Chairman KASICH. No, go ahead.

Mr. LARGENT. I just want to give you some examples of real things that are happening in Tulsa, OK, and Broken Arrow, OK, that deal with HUD and get you to respond to the changes that you are proposing and how they will impact what is happening in my district.

The first is, in Broken Arrow, OK. A developer from Ohio wanted to come in and take advantage of section 8 housing and section 142 benefits from the government and build a project that, first, was not needed in Broken Arrow, and second, was not wanted. But, because of certain tax provisions and advantages that he would have in building this, he was pressing forward with it. A huge battle ensued with Broken Arrow officials. As a result, at least, the latest that I have heard, is that it will now be built. It was wrong for a lot of reasons, but I would like for you to respond to that.

The second one is that I had an opportunity to tour around with the Tulsa Police Department from about 10 until 3 in the morning, and the tour that we took, looking for crime, was public housing. There was one particular development called Sun Gardens. It is a project that was built in South Tulsa. There have been about five people murdered there in the last year, year-and-a-half. It is crime-ridden. In fact, the police refer to it as "Gun Gardens", not "Sun Gardens".

Their response was, and, again, I am just telling you what they told me, because I don't understand it totally myself, is that this is not a bad idea. The problem is, all they do is put all these people together and there is no really any diversity in the population there. It sort of breeds crime.

Mr. CISNEROS. Right. Congressman, first of all, the program that you described that the gentleman came to Broken Arrow to build sounds like a program that doesn't exist anymore. I don't know

what the timetable of that was, but the use of project-based certificates in that way, when it goes against the market sense, wouldn't exist under the reforms that we are proposing. So I don't think you would find that kind of circumstance, where someone is coming into a market where the housing is not necessary, as you say, and not wanted, and be able to do it, because it simply wouldn't be possible.

Thank you for the second question, because it really does allow me to talk in direct terms to you about what we are trying to do with public housing. In too many places in America today, if you go to the police department and you were to look at a map on the wall and see with red pins the highest frequency police calls, they would be public housing settings.

There are a lot of reasons for that. The Federal Government is certainly an accomplice. Over the last 20 years or so, we put a preference on the very poorest of the poor in public housing and not mixed-income families. In other words, we have lost the sense that public housing could be a beginning place for working families who could then go on and do better in life.

But I can tell you, there are some wonderful stories in America from 30 years ago of people who grew up in public housing, like Bill Cosby and Kenny Rogers and Whoopie Goldberg and Isaiah Thomas. It just goes on and on and on, people who grew up in public housing 30 years ago.

But today, thanks to our preference rules, saying you must take all of the homeless and put them at the top of the list, or all of the people who are the very poorest and put them at the top of the list. We have come close to destroying public housing as a place where that kind of ladder of opportunity can exist.

So what we are saying is, instead of subsidizing units from now on, under these reforms, we will subsidize individuals, families, and they can make the choice as to whether they will stay or whether they will live somewhere else in the metropolitan area.

That is a really profound change, but it requires something very special on the part of the Republican leadership of our country, and that is an acknowledgement that if we are going to try to mimic the market, which is what this does, then we really have to make the marketplace open, so you cannot destroy fair housing strategies or open housing strategies, as some would do in this era. Otherwise, what happens is we give people a certificate, but they cannot, because they are African American, because they are black, live in a suburban setting or elsewhere in the metropolitan area.

So there is a duality to this that must be part of our solution. We want to recreate a market discipline, give people a chance to move, break up some of these concentrations, try to get mixed-income settings in public housing. But, we also have to be honest in saying, today, with discrimination existing as it does, too many people really don't have that choice, and that's part of the reason why they're concentrated.

But the Federal Government has been a great big part of the problem. We are going to solve that part of it, we think, by changing the dynamics and the rules.

Chairman KASICH. We have 6 minutes until the vote.

Mr. LARGENT. I am through asking questions. The only thing I would like to add to that is that I also read some of the things you had said earlier in the summer about economic diversity and actually placing low-income folks in high-income units, where they were given subsidies of $1,600 a month and had swimming pools and all that sort of stuff. It was in an article in the Wall Street Journal.

Mr. CISNEROS. I know that article, but——

Mr. LARGENT. That is not true?

Mr. CISNEROS. It was a fellow named Bovart, and he really did a job of sort of taking some absolute extremes of what it would take, for example, to get a four-bedroom apartment for a family in Manhattan and calling that the cost that would apply in Broken Arrow. That is not true. I can refute that article. In fact, I will get you a paper in which we refuted it.

Mr. LARGENT. Thank you.

Chairman KASICH. Mr. Secretary, this has all been very interesting. We have a vote.

Mr. CISNEROS. I understand.

Chairman KASICH. I want to let you get on the road. I look forward to that paper. We want to walk through that, as well, over here.

I love to listen to you. You are a great salesman. We are still some way apart, and who knows where we are going to end up at the end of the day, but I want to thank you for being here today. We will get together again sometime soon.

Mr. CISNEROS. Mr. Chairman, let me thank you, if I may, for your granting us the privilege to come over and have this discussion with you. We think it is very important to go beyond budgeting to some of the ideological and policy questions.

Chairman KASICH. That is right.

Mr. CISNEROS. Thank you, Mr. Chairman.

Chairman KASICH. Thank you, Mr. Secretary.

The hearing is adjourned.

[Whereupon, at 3:41 p.m., the committee was adjourned.]

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